

Retirement Adequacy

...has always mattered the most
and can no longer be ignored

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*This PDF does not
contain the animation
shown in the flash version.*

*Please find the ABCorp 401k Plan sheet
and review the instructions.
You'll be asked to follow those instructions shortly.*

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Session
focus...

How to help
401k novices begin
acquiring the **knowledge** and
personal motivation
to accomplish the **difficult task** of
accumulating enough money for an
adequate retirement income
by **starting early** and
contributing enough.

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Retirement
Education
Simulation

Follow the instructions on
the ABCorp 401k Plan sheet.
Toss your savings contributions ball
and hit your target.

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You just
experienced
the
prevailing
approach to
retirement
education

You had an opportunity to succeed...
But without knowing how to set and hit
your target, is it really an opportunity?

You had encouragement...
But without it being personally
meaningful, is it really encouraging?

You were told what to do...
But without personal motivation,
is it likely you'll do what you're told?

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How well has the prevailing approach been working?

87% of plan sponsors say most of their employees will **not** be financially prepared for retirement.

(Deloitte/CEBS)

'401k plans are **not** working well as retirement plans.'

Fred Reish
(PLANADVISER magazine 'Legend')

Half of 401k participants between 50-59 have less than \$30,000.

(Wells Fargo)

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401k retirement education is the largest failure ever of any adult-education effort

Devastating financial results

\$260 a month: what near-retirement employees can expect from their typical 401k + IRA accounts

[4% of \$78,000 / 12] (Center for Retirement Research)

\$1.2 Trillion: modest estimate of the education failure...if 1/3 of the 50 million 401k participants (16.5 million) don't learn the basics of using a 401k ...have a \$5,000 a year (\$416/month) 'shortfall' for 15 years (65 – 80).

[16.5 million X \$5k X 15 = \$1,237,500,000,000]

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Have we been doing retirement education wrong for 30 years?

Fire

some money into a 401k until we're nearly...

Ready

to retire...then we learn our

Aim

was far short of the amount we need...and it's too late to fix it.

A retirement adequacy test every employee should pass...

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What's the highest-priced purchase you may ever make?

If a person stops working at 65 and expects to live to 90 [how many years **25** ?] and wants to spend **\$40,000** each year, that's [**25** years times **\$40,000**] **\$1,000,000** of income.

More than your house?

'Wow, nobody explained it that way before.'

Do you feel the need to improve this example by using 'the way' that's always been used?

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Because
that's
'the way'
everyone
does it

'The way'
adds social security,
historical investment performance,
longevity, inflation, annuity rates,
replacement ratios...
and uses
factors and assumptions
concealed from view in
complicated projections
to calculate a
more 'precise'
– yet mysterious – number.

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Because
that's
'the way'
everyone
does it

**Yet the
'the way'
has failed.**

It's information
most 401k beginners
don't understand,
don't find motivating,
don't believe
and worse – don't use.

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What's the biggest obstacle to achieving retirement adequacy with 401ks?

401k plans are *ok...*
even bank savings accounts could work for retirement.
Is the critical problem ***operator error...***
like putting first-time drivers in race cars, wondering why they crash... then lecturing them on racing physics?
Do your 401k operators
– **your employees** –
know how to use the plan successfully...and avoid crashing?

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How did we get where we are?

Everyone wanted 401ks in the early 1980s...
Employers wanted lower costs, easier admin, relief from DB plans.
Employees wanted tax-advantaged accounts with 'opportunity for \$100,000+.'
DB plans were under appreciated.
Mutual fund industry wanted more customers.

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How did
we get
were
we are?

In the early 1980s...

The Peter Lynch
Fidelity Magellan Fund era.

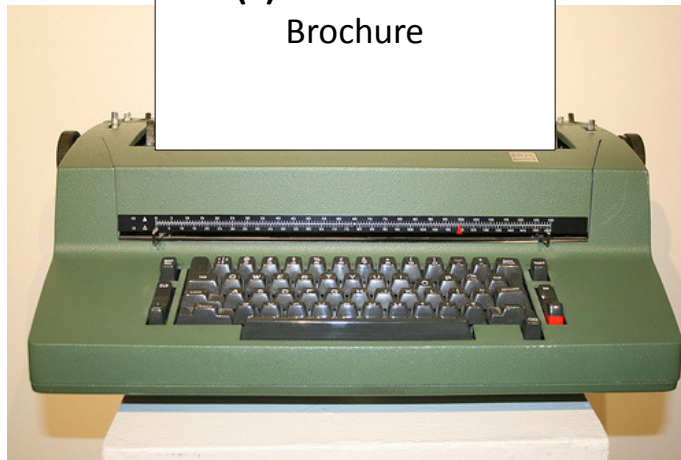
From 1977 to 1990, it
beat the S&P 500
11 out of 13 years
and averaged
29% annual growth.

That's what everyone wanted.

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With a few
keystrokes
...and
***no
malice***

401(k) Retirement Plan
Brochure



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401ks
were built
with parts
most
employees
were not
accustomed
to using

supplemental thrift plans

...the 'dessert' of the
DB pension 'full-course meal.'

mutual funds

...for people with pensions,
above-average wealth and
basic understanding of investments.

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It seemed
like a
good idea

But the new 401k approach...

Not pilot tested.

Not modeled after successful programs.

Not studied by adult-education experts
to ensure typical employees could
use the plans successfully.

Not reviewed by Congressional
committees or federal agencies.

...because everyone wanted it.

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The trend quickly became the norm

In early 1990s...
401ks were being surveyed for 'best practices'...and 'benchmarked' based on other employers' **plan provisions and services.**

Employee outcomes have never been the focus of 401k plan designs, federal regulations or **participant education.**

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401k benchmarking should compare your employees to successful 401k users

Employees 55 and older with **\$1 million accounts** (top 2%ers) had 'high contribution rates' and 'constant participation' (EBRI)

They **started early**, **saved a lot...** **never stopped.**

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401k
benchmarking
should
compare
your
employees
to successful
401k users

Why don't novice employees understand what to do...and do it?

They've been getting an **investment** education...
not a retirement savings and
income consumer education.

Shouldn't graduates of basic 401k retirement education be great at

starting early,
saving a lot and
never stopping?

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Today's
retirement
education
evolved
from selling
– not adult
education

401(k) Retirement Plan
Presentation



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Today's retirement education evolved from selling – not adult education

Mutual-fund sales presentations were:

- Designed to sell mutual funds to somewhat motivated and financially savvy potential customers
- Based on the selling approach of an expert **telling people what to do.**

Unfortunately...

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'Telling' is **ineffective** for unmotivated, non-financially savvy adults ...most employees

2400 years ago, Greek philosopher Socrates demonstrated *telling* doesn't create learning.

Adult education experts say '**telling isn't teaching**' ...adults must be motivated to learn.

Defenders of today's retirement education:

If the approach used for 30 years of having experts tell 401k beginners what to do was viable, shouldn't it have worked by now?

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New retirement world reality

Individual employees are fully responsible for their own adequate retirement income.

- After trying everything else
- ‘telling,’ auto-everything, target-funds, nudging etc. – isn’t time to help 401k beginners acquire the **motivation** and **knowledge** to **start now, save a lot, never stop?**

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There’s
proof
I don’t
know
exactly
what I’m
talking
about

Apparently, no one does.
‘...a systematic method
of evaluation of financial literacy
programs (retirement education)
does not exist.’

(Financial Literacy and Education Commission)

**There is no universal definition
of retirement education,
and no agreed-upon content.**

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If retirement adequacy is part of the purpose of your plan...

Plan sponsors have the **obligation** to ask education providers...
'When the education you provide is working well, what will employees know and how will it be measured?'

Otherwise, how can you measure the progress of your employees and the value the provider?

If retirement adequacy is part of the purpose of your plan...

My definition:
'Ensure employees before age 30* acquire the basic knowledge needed to begin using a 401k successfully.'

* 25 would be better.

Education providers have their own definition.

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Achieving retirement adequacy is about achieving a personal goal.

Humans do not voluntarily achieve **difficult** personal goals they have not personally set.

How difficult?

80% of financial pros say **save 17%** – including employers' \$ – throughout working career. (Principal Financial)

Wait to age 45, **save 31%**. (Center for Retirement Research)

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Benchmark
education
with what
winners
have

People who accomplish difficult things – run marathons, climb mountains, earn advanced degrees, save lots of money – have:

- 1. A specific, personal, meaningful goal** that they understood, defined and measured...and over time, improved with advice they trusted.
- 2. Desire and motivation** to learn, to improve and to do what's necessary to achieve the goal.

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Benchmark
education
with what
winners
have

Successful people have:

3. Meaningful learning experiences

to understand the content and trust the new knowledge they acquire.

4. Confidence they can succeed – but

realistic assessment of the difficulty

(believing it's easy significantly increases the odds of failure).

(Harvard Business School)

5. Perseverance to keep doing what's difficult when things get tough.

Is your education program instilling what winners have?

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What
can
employees
do using
401ks?

In simple, practical terms...

Price – define the financial lifestyle they want and the account balance it costs.

Contribute – fund the account to buy that lifestyle.

Invest – help fund the account.

Receive – create an income flow to last a lifetime.

It's what actuaries and fund managers do for DB plans...now employees are responsible to do it for their 401k – an **individually defined benefit plan.**

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Helping employees discover the **price** of retirement adequacy

Most people know how much money they spend and what things cost today. Use that to help them discover their **realistic, personally meaningful** price for retirement... **what 70% admit they've never tried to calculate or guess.** (about half who've tried cannot state any amount)

(Lusardi & Mitchell)

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Discovering the price

Imagine you were 'fast forwarded' to your last day of full-time work – and things cost the same as today:

How much do you want to spend each year.....\$_____

Compared to today, the same, more, or less?

How many years might you need the income...X_____

Example: Age 65 to 90 = 25 years

Your personal estimate...\$_____

Is this advice...or just 5th grade math?

Is it realistic?

More personally meaningful than an expert's replacement ratio?

Still feel the need to tell 401k beginners 'the way'?

Discovering the price

Imagine you're 65 today – it's your last day of full-time work – and you have \$100,000 in a account.

Let's say you want your account to provide income from 65 to 90 – that's how many years? 25

If you divide 25 years into your \$100,000 account, that's \$4,000 each year.

Advice...or 5th grade math?

Is it realistic?

*Will employees think,
'Gee, if I want \$20,000 each year,
I'd need **five** \$100,000 accounts.'*

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What matters most in getting 20 and 30 year-old employees started?

All are important...

Price Contribute
Invest Receive

Which is the least important for 401k beginners?

Which is emphasized the most?

(Is it because it's most interesting to the people hiring the education provider...and to the person delivering that content?)

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What matters most in getting 20 and 30 year-old employees started?

Investing doesn't matter as much as:

Price – no personally defined account target = no personal motivation.

Contribute – no contributions = nothing to invest...early on, contributions grow accounts more than investments.

Receive – no knowledge of how long account will last = no understanding of how much to save...or why not to take money when changing jobs.

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Contributing trumps investing

Morningstar...

‘The most important thing we can do is encourage participants to save more.’

Putnam Investments...

‘Saving more is the most powerful way to end up with more. Searching for the perfect fund or allocation is a far less effective approach.’

Simple math...

For a 401k beginner earning \$30,000 with \$6,000 account:

2% bigger contribution (\$600)

5% higher earnings (\$300).

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What would the inventor of Modern Portfolio Theory do?

Dr. Harry Markowitz – how he invested for retirement...

‘I visualized my grief if the stock market went way up and I wasn’t in it – or if it went way down and I was completely in it...so I split my contributions 50-50 between bonds and equities. I wanted to minimize my future regret.’

(TheStreet.com)

He won a Nobel prize for his theory
...but didn’t use it for his investments.

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Helping employees discover how much to **contribute** today

Perhaps the hardest to simplify.

After setting an account target, employees can estimate how much needs to be contributed each year.

Early in their careers, employees may not be able to contribute the calculated amount...but is it a realistic amount?

Employees with big income expectations will get a dose of reality...may need additional investments outside the 401k.

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Discovering how much to contribute

You can roughly estimate how much to contribute each year by dividing your target by the number of years you expect to work full-time.

Let's say Taylor intends to work full-time to 70
...is currently 30...and has a target of \$300,000.

70 minus 30 equals 40 divided \$300,000 equals \$7,500
age to end full-time work current age years remaining into Savings & Investment Target estimated annual contribution

Good news – employer contributions!

Plus possibility of compound earnings...and your larger contributions later in your career.

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Helping
401k
beginners
put
investing
in
perspective

Provide basic information about
stocks, bonds and cash.

Focus on what employees control:
contributions and diversification
...but not market changes.

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Why
401k
beginners
need to
know about
**retirement
distributions**

Knowing how much income
an account can likely pay for a lifetime
helps employees understand the size
of the account they'll need.

Many experts say withdraw only **4%** of
initial balance to have lifetime income.

Most people think **10%** is ok. (Wells Fargo)

It's tough to understand – even
Peter Lynch said 7%...then 5%
when the Trinity Study showed 4%.

**Employees should learn
this at 30 – not 65.**

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Remember
this?

If you expect to live on \$100,000 for
25 years, divide 25 into \$100,000.

That's \$4,000 a year.

What percent is \$4,000 of \$100,000?

(\$4,000 divided by \$100,000 is **4** %)

By helping employees discover
\$100,000 is expected to provide
\$4,000 a year...\$333 a month,
you can ask, 'How many \$100k
accounts do you need to have
the lifestyle you want?'

Advice...or just 5th grade math?

Many essential adult education elements are missing from today's retirement education

To succeed, **content** must be:

- received by **motivated learners** (*you cannot teach unmotivated adults*),
- **trusted**,
- **believable** based on their experiences and knowledge, and
- **explainable** by the person receiving it.

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Many essential adult education elements are missing from today's retirement education

The most powerful ingredient in adult learning: **motivation to achieve.**

Experts **telling** unmotivated employees, 'Here's your Monte Carlo simulation – and using replacement ratios and gap-analysis calculation.' – may be perfect information.

But because it won't be used, it's nearly worthless.

Yet it's priceless when motivated learners **ask** for this information.

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If employees don't trust the messenger, will they trust the message?

Who do employees trust?

3% say investment companies.

85% say their employer has their best interest in mind. (EBRI/MGA)

Are trusted messengers sending your 401k messages and offering advice?

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They **can** handle the truth

In today's economy, now is not a good time for employees to discover the enormous price of retirement

...but now is better than later.

The retirement industry's approach of hiding the realist cost of retirement is cruel and unconscionable.

It steals employees' time and opportunities to save that they can never get back.

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They
can
handle
the truth

'Rather than giving up, workers who have calculated how much they need are more likely to be very confident about having enough money than those who have not made a calculation.

44% of those who make a calculation took action...59% of them saved more.'
(EBRI/MGA)

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They
can
handle
the truth

No one can know exactly how much an employee's retirement will cost.

But employees can make realistic estimates...and talk with an adviser to get a more sophisticated opinion.

Here's why there's
no precise number...

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‘How much money will I need?’

Unfortunately, if you’re run over
by the party bus at your
‘last day of full-time work’ celebration,
you’ll need around **\$0** future income.

Or...

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‘How much money will I need?’

If you want generally the same standard
of living that you have now...and you
stop working full-time at 60 and
live to 102 (42 years), you may need
**more money than you made
in your entire working career.**

One million Americans in their 50s today are
expected to reach 100. (National Institute on Aging)

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They
can
handle
the truth

74% of employees plan
to work longer
to make up for small accounts
...but that might not happen.

45% of retirees were forced
to retire early (63% health reasons,
23% job vanished, 18% family matters)

Only 23% of current retirees
actually work (health, job issues, etc.)
(EBRI/MGA)

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Content
must be
understood
by the
people
receiving it

Monte Carlo simulations and
efficient frontier plot points
are effective with financial pros.

But they don't attend
basic 401k presentations.

Shouldn't plan sponsors fire any
retirement educator who is telling
401k beginners about
efficient frontier...alpha...beta...yield...
Sharpe ratio...present value...P/E...
dollar-cost averaging...or any
investment terms requiring a glossary?

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Content
must be
understood
by the
people
receiving it

It must make sense to people who
struggle to figure a gratuity.

**In basic retirement education,
allow only simple explanations
that employees are
able to explain back to you.**

Build on what employees know
...simple math and life experiences
like shopping and buying things.

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Content
must be
understood
by the
people
receiving it

Why not show how buying future
financial income is like other purchase:

Retail price – total needed if
'fast forwarded' to your last day
of full-time work.

Discounts – amounts already paid
(current savings, projected pensions,
saleable assets, social security and any pay
earned working after your full-time career).

Layaway payment – additional
amount needed to purchase your
future income target.

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Your financial future...a realistic guesstimate

Your estimated **retail price** of future lifestyle income

$$\begin{array}{rclcl} \underline{\$48,000} & \times & \underline{25} & = & \$1,200,000 \\ \text{annual spendable} & & \text{years} & & \end{array}$$

Your estimated **discounts** – what's already paid

– Current single sums (401k, personal savings, etc.) – \$54,000

– Lifetime payments (pensions and social security)

$$\begin{array}{rclcl} \underline{\$19,000} & \times & \underline{25} & = & -\$475,000 \\ \text{annual benefit} & & \text{years} & & \end{array}$$

Your estimated additional **layaway** = \$671,000

Is this a realistic estimate that's personally meaningful and understandable...that they could explain back?

Still think 'the way' is good for 401k beginners?

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Behavioral finance is insightful... but can naive employees be 'nudged' to success?

Auto-enrollment is 'anchoring'
70% of auto-enrolled employees at **3%**.
(Mercer)
40% would have elected higher rate!
(AON Hewitt)

Employee who has no idea of the cost of retirement has been auto-escalated to 12% contributions...learns if she drops to 6% (gets full match) has extra \$200 a month to get her Ford Mustang dream car rather than a Ford Fiesta.

Isn't **knowledge** essential?

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Advice

Most employees will need advice
...but it's valuable only if it's used.

Only 6% with online advice 'used' it.

(Hewitt)

**Advice must be sought (pulled)
...pushing it doesn't work.**

Let's help 401k beginners succeed
in building sizable accounts and
becoming more sophisticated
retirement income consumers...
who see the value in professional
advice – and want it and use it.

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What can you do to
strengthen retirement adequacy
in your 401k?

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What you
can do

Key Step: Commit that every employee
over age 25 can answer and explain:

1. What's the realistic **estimated dollar amount** I'll need to have the **future financial lifestyle I want**?
2. How much money should I be **contributing today** to reach my goal?
3. How should I be **investing** to help reach my goal?
4. How will I make sure **following my full-time career that income from my account will last as long as I live**?

Require your educators make this happen.

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What you
can do

2. Require educators to define 'what's the **least** 401k beginners must know to get a good start building the realistic financial future they want?' And how will that be measured?
3. Hire an adult ed expert to assess the program's techniques or ask the provider for proof their teaching techniques work...or at least Google 'adult education principles' to see how many are used in your retirement education.

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What you
can do

4. Involve your financial staff in evaluating education and advice for employees over 40 or who have \$50,000 accounts...
but not for 401k beginners.
5. Ask your provider how they ensure employees trust the provider's people and communication materials.
6. Send employees missing the full match a 'how much you lost by not contributing 6% each paycheck' letter.

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What you
can do

7. For plan success measures, use midpoints/median (\$12,655) – half have less...half have more.
Avoid averages (about \$46,000). (EBRI)
8. Discuss incentive fee performance levels...for example, full fee if certain success level is reached, X% less if not, X% bonus if exceeded.
9. If most of your employees do not have the knowledge needed to operate a 401k successfully, ask senior leaders and ERISA counsel if the organization has any responsibility...or liability?

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In closing...

Focus on getting more 35-year-olds
– and fewer 55-year-olds –
with \$50,000 balances.

**Celebrate progress – recognize
employees who have set their
realistic account targets –
(you don't need to know the amount)
award pins, ribbons,
certificates or cash.**

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In closing...

Don't ***tell*** employees what to do
...help them discover it.

Be open to ideas...at least 'new ways'
are not proven failures.

If the current voluntary
401k approach to employer-sponsored
retirement plans can't provide
success for the majority of employees,
find one that will...

America's workers deserve no less.

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Retirement Adequacy

...has always mattered the most
and can no longer be ignored

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