# Answers to the 401k Questions that Matter Most

***And probably aren't in your employees' communication materials.***

By Dennis Ackley

Maybe there wasn't enough room in your employees' 401k booklet. Or maybe whoever wrote it focused too much on investing – not enough on helping employees begin using a 401k to have the financial future they want. So here, in *Jeopardy* style, are six answers employees need – followed by the questions.

## *$333 at age 65.*

***That's the answer to, "At age 65, about how much can employees who have $100,000 in their 401k account expect each month for as long as they live?"***

Repeat aloud: $100,000 at 65 assures around $333 each month. That's what many experts say. It's four percent of the account for the year (4% of $100,000 is $4,000, divided by 12 months is $333). A few experts say it's closer to $167 a month (2% a year). Some say as much as $417 (5% a year).

**Isn't it better for employees to know this today rather than finding out when they're ready to end their full-time career?**

Employees should ask the plan's representatives about the withdrawal rate they recommend. Employees should also ask about withdrawal techniques and annuities that could provide somewhat more. Of course, employees need to understand the advantages and disadvantages of their financial choices.

## *Not their house.*

***"What's the most expensive purchase employees will ever make?"***

The total price of employees' income following their full-time work will likely be much more than the price of their house.

Let's say they want $40,000 annual income starting at 65 and lasting to 90 – that's 25 years. Simple math: $40,000 times 25 equals $1 million. Yes, one million. If they want more income, or want it for a longer time, or if inflation out paces their investments, the price will be higher – maybe a lot higher.

Here's good news. Along with their 401k, income from Social Security, any pensions, personal savings, and part-time work will help employees pay for this purchase. Working full-time longer also reduces the price.

*Why are these points not covered? Is it because the communication is overly focused on investing …not on defining, pursuing and achieving a personally important future financial goal?*

## *The number won't be exact.*

***"Can an expert or software program tell your employees exactly how much money or 'the number' they'll need for their future?"***

Here's why it won't be precise. A key part of estimating the number is entirely up to individual employees – the future lifestyle they want. If today was the last day of their full-time working career, would they want a continued lifestyle that's half as much as they spend now, twice as much, or the same as they spend today? It's their future, their life, their decision.

How long they'll need the income is another key element. To highlight the impact, here's an exaggerated example. If, God forbid, an employee is run over and killed by the party bus when celebrating his or her last day of full-time work, that employee will need around…$0 future income.

At the other extreme, an employee who stops working at age 60 and lives to 105 will need 45 years of income. That's longer than he or she worked…and probably more money for that income than was earned in a lifetime of work.

Although the number can't be exact, employees should talk to experts and use computer programs to get a good estimate of the likely range of the cost.

## *Only four.*

***"How many things can employees do with their 401k to help assure an adequate income when their full-time career ends?"***

1. **Define the future lifestyle the individual wants**…even though it cannot be determined precisely, all employees need to set a personal dollar goal for their 401k account.
2. **Contribute**…starting today, employees should put into their account an amount from each paycheck that's aimed at reaching their goal – with some help from their investments and any contributions from their employer. In most cases, employees will have more income to save later in their careers.
3. **Invest** wisely...have a mix of different investments (what the pros call 'diversification') and a long-term strategy – it's money the employees may not be spending for 20 to 40 years.
4. **Receive income**…take money out of the 401k account only after the employee's full-time career ends…and in a manner that assures a lifetime income.

Employees need a dollar goal that's personally relevant to them. Otherwise, there's little chance they'll succeed. Naturally, they may change their goal over time. Their future plans and aspirations may change. Inflation and a host of other things could change. But they cannot focus on hitting a target if they don't have one.

Investing is important. But during the first several years that employees have an account, investing is not as important as contributing. If employees don't contribute, there's nothing in their account to invest, nothing to grow.

Every day they wait to start contributing is a day they'll miss any contributions from their employer and the opportunity for compound earnings. The larger the account gets, the more compound earnings matter. That's money earned on the contributions plus – here's the kicker – it's money earned on the money they've already earned.

The dangerous part of not contributing today is that if employees wait they may never be able to afford the future lifestyle they want.

Consider this. Will employees be able to build up a 401k account in their last 10 to 20 years of work to support the lifestyle they want for 20 or 30 years when they no longer want to work – or are unable to work? At that time, if they don't have much in their 401k, they may have only whatever Social Security pays. They may need to turn to their children, their community or the government for more. Again, it's their future, their lives, their decision. Good or bad, that's the 'system' for millions of Americans.

Of course, if employees pocket their 401k money when they change jobs, none of this matters. The money they take out during their working career is money they won't have when their working career ends.

## *Employees are getting what they pay for.*

***"Whose money is paying the organizations that run your 401k and manage the investments?"***

In most cases, it's the employees' money. The fees are taken out whether their accounts go up or down in value.

For every $1,000 employees have in their accounts, they could be paying around $5 to $15 each year…or even much more. The fees pay for the management of the investments, plan administration, printed materials, websites, statements, retirement educators, phone representations and most other aspects of the 401k.

The 401k representatives should be able to tell employees how much they are paying.

Employees may be receiving good value for these fees. But if they are not satisfied with a service, employees should tell the plan administrator – they're paying for it.

Different investment options usually have different fees. Certainly, some good performing investments have higher fees. And perhaps some equally good ones are lower priced. As in making any important purchase, employees need to be smart shoppers. They should know what they want, what they're buying, what the cost is and what outcomes they should expect. Then, over time, they should make sure they're getting what they're paying for.

## If they could see the future, they'd be picking the winning lotto numbers.

***"Why won't investment professionals tell employees which investment will turn out the best."***

Too many employees may have unrealistic expectations. Investment advice from even the smartest investment experts is a guess – probably a very sophisticated, intelligent guess. But not a guarantee.

At a minimum, a good investment advisor can help employees plan better and avoid dumb mistakes. Most advisors can help employees do much more.

To some extent, investment advice is based on what certain investments have done in the past and what the experts think the investments will do in the future. But what worked in the past may not work in the future. And what experts predict may not happen.

That's why most advisors encourage employees have a well thought-out, 'diversified' mixture of different types of investments. Advisors can help employees decide what mix they want of investments that are expected to do well when the market goes up…and the ones that are likely to remain generally stable even when the market goes the other way.

Employees are purchasing their future lifestyle. They should know the basics of the investing. They should also know enough about any advisor they use to judge if he or she is working in their best interest. Even if employees are using a pre-mixed investment fund or a target fund – or a computer program that's providing advice – the employees should be confident that the approach is aligned with their needs, objectives and emotions.

## These answers are just a start

With these answers, employees would know how to ***begin*** using a 401k to achieve the future financial lifestyle they want. They'd know:

- roughly how much money they'll need to help pay for the largest purchase they'll ever make – but the price is impossible to calculate precisely,
- the four things they can do with a 401k,
- they are paying for the plan, the investments and services, and
- no one knows for certain which investments will be 'the best'…but good advice is a good investment.

Perhaps most of all, employees would know they're in charge of their 401k and their future financial lifestyle. So they should start now acquiring additional knowledge and advice so they can define, pursue and achieve it.

**Did You Notice?**
There's a reason that 'retirement' was never used in this article. Younger workers avoid information connected with the word. Too many older employees hide behind the rationalization that they'll never retire. Yet both of these audiences need to know the answers highlighted above.

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For 20 years Dennis Ackley has been an advocate for clarity and accountability in retirement education – helping workers gain the knowledge to achieve the financial future they want. His award-winning communication programs on retirement, investing, and health care have reached three million employees at hundreds of employers. For more articles and more information, visit ***www.DennisAckley.com.***