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retirement-insight.com/march-2018-infre-update/

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- Describing the importance of independent accreditation of the CRC® program, how it was created in 1997 with Texas Tech University, one of the leading financial planning programs in the country, with over 100 professionals from all corners of the retirement industry to ensure that Certificants meet a minimum competency standard for fulfilling their responsibilities as retirement counseling professionals.
- Stating how you are required to maintain up-to-date, retirement-specific knowledge by submitting proof of completing 15 hours of continuing education credit each year.
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How to “Pensionize” Any IRA or 401(k) Plan

retirement-insight.com/how-to-pensionize-ira-401k-plan/

By Steve Vernon, F.S.A., Research Scholar, Stanford Center on Longevity

I worked at Watson Wyatt Worldwide on the front lines of the transition from defined benefit and contribution plans in the private sector in the 1980s, 1990s, and the turn of the century. I always thought it was not a good idea to ask individual workers to be their own actuary and investment manager. However, I feel like we are making progress on adequate savings now through default options.

In my encore career now in the research role at Stanford, I have been focusing on de-cumulation, or how you can deploy savings in retirement. Moreover, we may have found one solution that is straightforward for many people to implement.

Steve Vernon, FSA – Expert in Strategies that Integrate DC Plans, Social Security, QLAC
Editor’s note: This article is an adaptation of the live webinar delivered by Steve Vernon in 2018. His comments have been edited for clarity and length.
You can read the summary article here as part of the 1st Qtr 2018 Retirement InSight and Trends Newsletter, worth 1.0 CE when read in its entirety (after passing the online quiz.)
You may also choose to take the full length course How to “Pensionize” Any IRA or 401(k) Plan for 1.0 hours continuing education (CE)credit.

Introducing the “Spend Safely in Retirement Strategy”

You start by optimizing Social Security. If necessary, you might need a portion of your savings as a retirement transition bucket, so that if you retired before you start Social Security, you could replace that Social Security benefit that you are delaying with savings. For middle-income people to do this strategy, Social Security might be all the annuity income that they need. The remaining savings, if you use the IRS required minimum distribution, can be in either a target date fund or a balanced fund which are quite common in 401(k) plans. This strategy actually compares favorably to more complex strategies.

Right up front I am giving away the solution, but then we will go into details. I want to say I acknowledge that there are many other viable retirement income strategies. I am not representing this as the perfect solution, which, by the way, does not exist. What we are proposing is that this is a straightforward solution that can work with many, many people, particularly middle-income retirees with less than a million dollars in savings, which describes lots of people.

When you are looking at financial strategies for retirement, there are at least two perspectives. One is a financial planning perspective, where a financial planner custom designs a plan to fit his or her client. For financial planners or people who can afford a financial planner or work with them, that is a great thing. What I am focusing on is this other perspective – the employee benefit perspective. This is the way retirees planned for retirement in previous generations. They elected a stream of retirement income from their retirement plan at work, and then they adjusted their budget to reflect the income that they got from the pension plan and Social Security. I am not saying this is ideal. As a financial professional I would rather use the financial planning perspective. However, we have to acknowledge this employee benefit perspective is how many people plan their lives in retirement. I want to help those folks.

Only about one-fourth to one-half of people work with professional advisors, and fewer than half try to calculate their retirement needs. This may not be ideal, but this is the way many people plan for retirement. Those people tend to fall into two camps, and we have surveys that support this. The first camp greatly fears outliving their savings, so they kind of hoard it and make minimal withdrawals. The second camp wings it; they are not even thinking about making their savings last for life. They use their savings like a checking account just to pay for current living expenses.

When you see the rate that those folks are taking the money out, it does not look sustainable to last the rest of their lives. The first camp might be able to spend more and still feel safe. The second camp actually needs to spend more safely so that the money lasts for the rest of their life. Few defined contribution plans offer more than installment payment plans or planning tools.

Plan sponsors to date have been hesitant to put retirement income options in their plan, worrying about fiduciary risk, costs, unsatisfactory market offerings, reluctance to offer just one solution, and complexity. The solution we are talking about today actually meets these common barriers. What I want to say to the audience today — I know some of you are financial planners — what we are showing is a technique that some of your middle-income clients might use, and you would offer your services to wrap around and do refinements from it.

Retirement planning involves tradeoffs.There is not a single perfect income retirement solution. The tradeoffs are what is the amount of income you expect to get throughout the rest of your life, how much wealth or liquidity you have — some people want to have bequests they can offer at the end of their lives — and implementation, simplicity, and costs. All of these involve tradeoffs.

We are not saying that there is a one-size-fits-all solution here. We are just acknowledging that there are many tradeoffs. For example:

- If you want to maximize the amount of income, that might be at the expense of reducing your accessible wealth or liquidity or reducing your bequests.

- Making sure the money lasts for the rest of your life — inflation, investment risk, also known as sequence of return risk, and death of a spouse — you want to make sure the money keeps going after one spouse dies.
- In later years cognitive decline or making mistakes or fraud — those are always problems.
- You want to minimize income taxes.

These are all the common risks that people might face. It is a lot to juggle, but I think that people are resilient. Moreover, if we can get simple solutions that address many of these risks and get people close to financial security, then it is reasonable they can adjust their living expenses budget from there. That is really the point of this strategy that we are talking about today.

Retirement Spend-Down Strategies

Most middle-income workers are going to be generating income from Social Security, pensions, spend-down from savings and possibly continued work. These are the mechanisms that employers can influence. However, people also have assets outside of employer-sponsored plans. They may be interested in reverse mortgages, small businesses, rental real estate, personal assets, such as life insurance, and other IRAs. We are just acknowledging that the first group is resources that employers can sponsor, but everybody is potentially going to draw from these other resources as well.

Spend-down methods that are common: you can have annuities with insurance companies, or you can have withdrawals from invested savings or some combinations. You also can take out just the investment income only and keep principle intact. That is a very conservative method that might work for someone who wants to leave a bequest and leave that income for a bequest. You can do a systematic withdrawal plan where you have some method that is withdrawing interest and principle systematically. Finally, you can do a payout just for a limited period. The challenge really is having a decision framework that will deploy all these retirement income solutions so that their savings and their income last the rest of their life.

We think the answer to this challenge is to apply modern portfolio theory concepts that we are so familiar with in the accumulation period to the payout period. When we are accumulating money, we talk about asset classes. In the payout period, we are going to talk about retirement income classes. We talk about asset allocation in the accumulation period, and now we are going to talk about retirement income allocation. In the accumulation period, we are focusing in on accumulating assets, and now we are focusing in on the amount of retirement income. Finally, while accumulating money, you really want to minimize investment risks, however you might define that. We want to, in the payout period, minimize the risk of income losses.

Retirement Income Studies by the Stanford Center of Longevity and Society of Actuaries

We believe that applying the language and concepts from modern portfolio theory, that has worked so well in accumulating money, those same concepts should apply in the retirement period. This has been a major focus of work at the Stanford Center of Longevity, and we have been collaborating with the Society of Actuaries.

Our 2017 study, *“Optimizing Retirement Income by Utilizing IRAs, Retirement Plans, and Home Equity,”* is the culmination of several other projects that we have done jointly with the Society of Actuaries. If you look at the statistics, roughly there is the same amount of money in employer-sponsored retirement plans as in IRAs. Then there is about as much money in retirement savings as there is in home equity. Everybody is a little different in that mix, but we think that Americans are going to need to learn how to integrate all three of these sources as they approach the retirement years. In this study we have taken a portfolio approach toward combining these different sources.

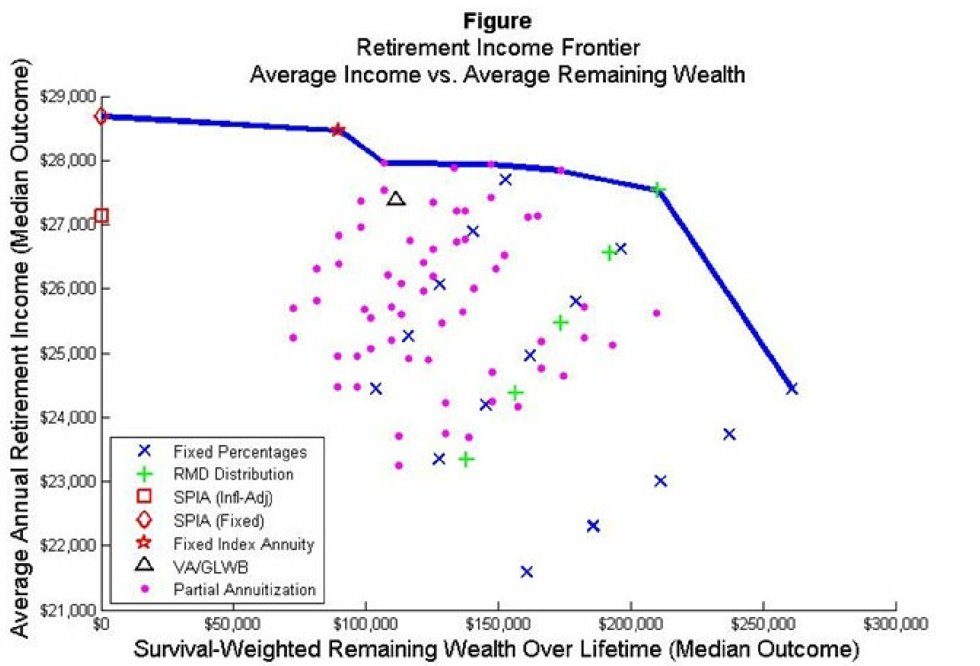
We put together a systematic comparison of different retirement income strategies and looked at viable solutions that are currently available in the DC marketplace, the IRA marketplace, and reverse mortgages. We are not dreaming up new solutions that are not available yet.

We assessed the tradeoffs that we talked about earlier to help us address what I call “what about” objections. What I mean by that is whenever I present retirement income solutions, someone raises his or her hand, and he or she says, “What about inflation?” or what about this or what about that. It can often stop the conversation. What we want to show is there are just tradeoffs. If you object, I say, “Okay, what is the solution that you are recommending? Chances are it is pretty good, but it is going to have its shortcomings as well.” To address these “what about” objections, we just need to look at many, many solutions and look at many goals that they might want to meet so that either the financial advisor or the retirement plan can help customize the solution to the specific goals of either the employee or the client.

In our study, we compared 292 different retirement solutions. We looked at three hypothetical employees who are age 65: a single woman with $250,000 in savings, a married couple with $400,000 and a married couple with one million. Now, let us say right here that these statistics are above the median for older workers; these are a more affluent group in the workforce. We acknowledge that there are many, many, people with savings less than this amount, and they are going to be challenged in their retirement years.

The 292 solutions we looked at included starting Social Security right away at 65 and delaying Social Security until age 70. We looked at single premium immediate annuities (SPIA), systematic withdrawal plans (SWP), including the required minimum distribution (RMD) from the IRS, and guaranteed lifetime withdrawal benefits, which is a hybrid annuity. We looked at fixed index annuities (FIA), which is another hybrid annuity. We looked at combinations of SPIAs and SWPs and FIAs and SWPS. Finally, we included reverse mortgages. We looked at lots of different types of retirement income solutions. That was the point of this study, particularly to address the “what about” objections.

Every one of these different retirement income solutions has different shortcomings that some other method might address better. Then some other method might have its own shortcomings. In our analysis, we used stochastic forecasts of income and accessible wealth. From that, we developed an efficient frontier showing the amount of income versus liquidity. These are powerful tools that defined benefit plans used to define funding and investment strategies. Our assumptions reflected the current low-interest rate environment. We also compared institutional pricing that you might get through an employer or a plan sponsor.



If you want more accessible wealth, going along the horizontal axis, that is going to come at the cost of reducing expected retirement income. This is the first analysis that we used to look at the 292 different strategies. From that, we looked at strategies that were either close to or near the efficient frontier.

We developed eight metrics to assess these tradeoffs. The first one is the amount of retiree income. However, we also did a second metric for inflation protection. Is the amount of income expected to increase in real terms throughout retirement, stay level, or decrease? The third metric was the average level of accessible wealth. The fourth metric was how quickly that wealth is being spent down. The fifth metric is the amount of bequest that might be left.

The last three metrics are very important, but they are not intuitively obvious. We measured downside volatility, meaning when the income goes down in real terms, how far down does it go? We wanted to measure downside volatility because we contend that upside volatility will not be too troublesome. Some of these measures of standard volatility mix in downside and upside volatility. We suggest that if your retirement spikes, you are not going to be complaining too much. We want to worry about downside volatility.

Then the last two measures we looked at are the probability that your income might fall below some absolute minimum threshold and what is the magnitude of that shortfall. Using these eight metrics, we came up with a retirement income dashboard, and this just shows one portion of such a dashboard where we would compare six different retirement income solutions graphically. I am just showing this to give you an idea of the kinds of data at which we looked. However, in this case, the last three are the retirement income solution that we are talking about today. The last three just have different allocations to stocks.

The first three are combinations of SPIAs and the RMD. It is showing an example of graphically how we compared these different strategies. Here, the turquoise bar is actually the amount of income that is either equal or more than others, but not dramatically so. You will see that the direction of income is beating others in inflation protection, and also in the last one on this chart, it has got the highest amount of accessible wealth. We are not going to get into detail here, but I am just showing you the level of detail into which we went.

Also, if you go to the full report, you will see this in all its gory detail. Here is another key point to understand this strategy. For most middle-income retirees, Social Security represents a substantial portion of their retirement income. We show twelve different retirement income strategies, and the colored portion is the part that Social Security income represents of their entire portfolio. What we are seeing is that anywhere from two-thirds to more than 80 percent of your income might be represented by Social Security. This is why it is important to optimize your Social Security income.

When you think about it, Social Security is nearly a perfect retirement income generator. If you optimize it through a delay strategy, it helps optimize your total retirement income. It protects against most common risks: longevity risk — it is paid for the rest of your life. It is indexed for inflation. It does not go down when the stock market goes down, and there is a survivor's benefit. Because it is paid automatically and goes into your account, it helps avoid cognitive decline mistakes and fraud. A large amount of Social Security is exempt from income tax for many people. No other retirement income generator has all of these advantages.

This is why we think optimizing Social Security for middle-income people is important. Our conclusion from our study was that optimizing Social Security before you purchase annuities or invest in fixed income SWP is best. You want to optimize your Social Security first because the return in optimizing Social Security expressed as an amount of retirement income is greater than if you purchase an annuity or invest in a fixed income SWP. Once you have optimized Social Security and you want more guaranteed income, then you want to consider buying an annuity or investing in bonds.

We are not saying do not buy annuities and do not buy bonds. We are just saying do not do that until you optimize Social Security. For middle-income folks, Social Security might be all the retirement income they need – anywhere from 60 to 80 percent of their total income is this Social Security portion – and it becomes the "bond" part of the retirement income portfolio. If you have 80 percent or 70 percent of your retirement income portfolio in guaranteed income, then the remaining could be invested in an easy to implement and systematic withdrawal plan with an aggressive asset allocation. Even though it is an aggressive asset allocation, you still have 60, 70, 80 percent in what I can "bond" parts in your retirement income portfolio.

What is the "Spend Safely in Retirement Strategy"?

I have also called it the "*SSRMD Strategy*" for professional audiences. You want retirement checks that are reliable, guaranteed for the rest of your life, will not go down if the stock market crashes, and those you can use to pay for your basic living expenses or at least get close.

Then you want to have some bonuses that have some potential to grow, but also because they are invested in the stock market that might go down. That is money you might want to use for discretionary living expenses like travel, hobbies, or supporting your grandchildren. The Social Security portion and annuities — those are your retirement paycheck. SWPs that are invested primarily in stocks become your retirement bonuses. The *Spend Safely in Retirement Strategy* Part One is optimizing Social Security — that is the retirement paycheck.

Most of the time you optimize by delaying for the primary wage earner as long as possible but no later than age 70. The best way to implement this is to work just enough in your 60s to enable delaying Social Security. However, we acknowledge that many people do not want to delay retirement until age 70. If you are retiring before and you are starting your Social Security benefit, you might want to set up a retirement transition bucket. That is going to replace the Social Security benefit that you are delaying.

In a very simple example, suppose your Social Security benefit would have been $20,000 per year at age 65. You want to delay Social Security to age 70, so you put $20,000 times five years, $100,000, aside and that is what you are going to draw down between age 65 and 70 that allows you to draw down Social Security at age 70. You would invest this retirement transition bucket in funds that are common in 401(k) plans, such as stable value funds, short-term bond funds, money market funds. Because of your short investing horizon, you do not want to invest this money in the stock market. We think a short-term retirement transition bucket is a good way to protect your income in the period leading up to retirement and as you are transitioning from full-time to part-time to full retirement.

Part Two, then, is from your remaining savings you are going to take the IRS RMD to generate retirement income. That is what is characterized as your variable retirement bonus. Our forecasts are showing that if you get good returns from the stock market and you are invested significantly in stocks, you will get a real rate of return and a real bump in your retirement income.

However, we acknowledge that many people may not want to go 100 percent into stocks with this portion, even though our analysis support that. Investing in the QDIA, either a low-cost target-date fund or a balance fund, is also a good way to implement this strategy. This strategy, I think, works best for workers with no significant defined benefit pension and having between $100,000 and one million in retirement savings.

If you have fewer than $100,000 in savings and you are in your mid-60s, that is a tough spot to be in, and I will say that strategies to deploy retirement savings do not work very well when people do not have enough retirement savings. The best options they have are to work longer, delay Social Security, and reduce their living expenses. I am not glorifying that. That is a tough situation in which to be. All I am saying is that retirement solutions from savings do not work for people who do not have savings. On the other hand, if you have more than one million that can justify using more refined methods. Working with a qualified and unbiased advisor might be a good thing to do if you are fortunate enough to have savings well more than one million dollars.

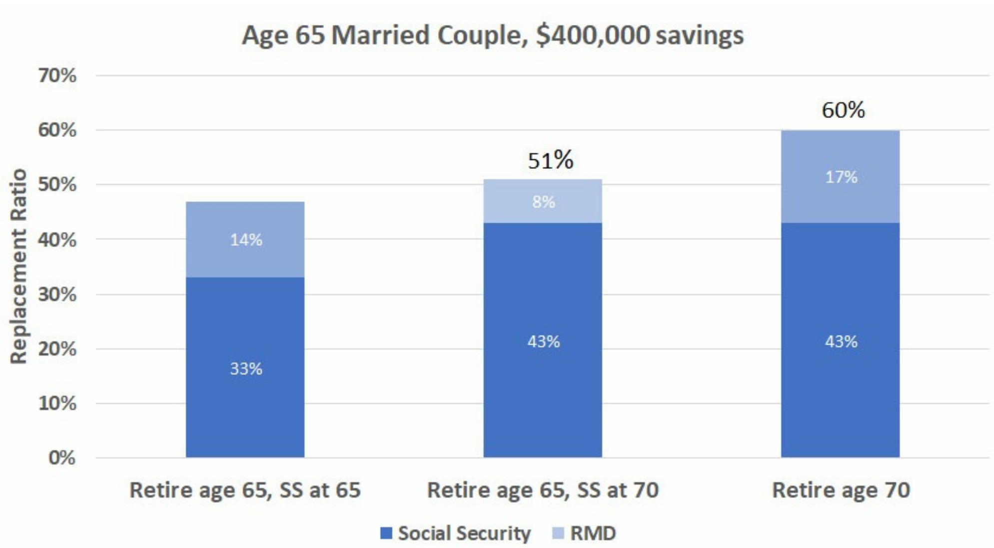
The *Spend Safely in Retirement Strategy*, compared to 292 other strategies we looked at, delivers equal or greater income throughout the life of the employee or retiree. It has moderate liquidity in bequests. It produces more liquidity in bequests than most annuity solutions. On the other hand, it produces less liquidity or bequests compared with pure systematic withdrawal strategies that do not use your savings to optimize Social Security. It provides low downside volatility. One reason for that is because Social Security is such a large part of your retirement income portfolio, any fluctuations in the remaining portion from the RMD are dampened and mitigated by Social Security.

It is simple to implement and low cost, and it does provide equal or greater protection against the common risks that we talked about earlier. These are the risks shown here. Let us just show one example. This is with a married couple age 65 with $400,000 in savings. The first bar just shows that if they retired age 65 and started Social Security age 65, the dark blue represents what they will get from Social Security and the lighter blue represents what they will get from the required minimum distribution.

The next bar shows they supposedly are still retired at age 65, but they use a portion of their savings to enable a delay strategy and delay Social Security until age 70. Now their total income goes up to $51,396, a $4,000 increase compared to $47,302. They are getting a pretty big pop in their retirement income. If they can work part-time in their mid-60s to delay Social Security and enable drawing down their savings until 70 and not have to use a retirement transition bucket, then they get an even bigger bump to a retirement income of $60,234.

This kind of information can help people decide maybe if I can just find part-time work I do not need to save any more money. All I need to do is delay Social Security and delay drawing down my savings. This becomes a viable strategy for people in their 60s that could improve their lives by having more time to pursue their interests, only working part-time, and enabling their Social Security and their savings to grow.

This next chart converts the dollar amounts shown on the previous chart to replacement ratios.



The dark blue represents Social Security again. That represents what I will call the bond part of your retirement income portfolio, the guaranteed part. This is showing why the light blue, if you invest that even 100 percent in stocks, you are still investing a tiny part of your overall retirement income portfolio in the stock market.

Now there is another conclusion to draw from here. Look at these replacement ratios. Even if you optimize Social Security and delay until age 70, they only have a 60 percent replacement ratio, which is less than what most common retirement advisors recommend.   This shows the dilemma that many people are facing as they are approaching their retirement years that they may need to reduce their standard of living significantly. Remember a married couple age 65 with $400,000 in savings is well above the median for workers that age. This is the challenge that is facing future workers that do not have significantly defined benefit pensions and only have savings. They are going to need to figure out how to live on a reduced standard of living. I am not saying this is desirable. I am saying this is the reality and collectively, this is one of the challenges that you are going to face with all your employees and your customers. I am thanking you for helping people face this challenge.

Refinements to the Spend Safely in Retirement Strategy

The *Spend Safely in Retirement Strategy* is a baseline or a guideline. There are refinements that you may find desirable. We are not advocating that it is a rigid strategy. It is really a way of thinking. From that strategy, you might have refinements.

For example, I think everybody should have some emergency fund that is not used to generate retirement income and that would be for unexpected expenses or maybe expenses you are expecting, such as you need to fix the roof or buy another car. You want to set that money aside and do not use it to generate income.

Think of a travel bucket. I hear some people say, “Yeah, I want to spend more money in the first ten years of my retirement while I am still healthy and able to do that. So, I would like to spend more money than what the RMD would throw off.” For example, suppose you want to spend $5,000 per year, in the next ten years, for travel. Set aside $50,000 and do not use that to generate income. Use your remaining savings to generate income, delay Social Security and do all the other things we have been talking about, and now you can travel in your first ten years of retirement. It is just an example, but it gives you an idea. Some people may want more guaranteed income, and so you might want to buy an annuity, either a SPIA or an FIA or a GLWB (guaranteed lifetime withdrawal benefit).

Some people may want even more, particularly they want more income, and if they have enough home equity they might want to take out a reverse mortgage line of credit that can supplement their income. That becomes another source of guaranteed income.

Finally, I have been talking about delaying Social Security until age 70. That does produce optimal results, but you still get plenty of boost if you delay Social Security until age 66 or 67 or 68. It does not need to be a rigidly applied strategy. This strategy, for you employer sponsors, addresses the common barriers that we saw earlier. It is simple to implement — low cost, really. It is just a communications cost.

The default payout option can be the IRS required minimum distribution starting at 70.5

coupled with the QDIA for people of that age. I think this offers fiduciary protection to plan sponsors, which is important. They already have fiduciary protection with the QDIA. Now when you are looking at the IRS required minimum distribution, if that is your default payout option, all you are doing is complying with the law. You are required to pay this out. It is hard to imagine plan sponsors getting in trouble complying with the law.

I think offering this as a default payout option can be viable for plan sponsors. Then a participant would make a positive election if they wanted to use some other payout option. This strategy uses current offerings. We do not have to invent anything new. It uses target-date offerings and stable value funds. Another benefit of this strategy is that it is very straightforward to prepare retirement income statements. There is much interest in plan sponsors generating retirement income statements for their participants, and the controversy that comes up is that you have to make assumptions about what product they are going to buy or what interest rates are.

In this case, we know what the rules are for Social Security, so you can show projected Social Security amount up to age 70. We know the RMD rules. You can assume what investment return you might make, or not. You can just say no investment return. It makes it very straightforward to prepare retirement income statements.

Other refinements: plan sponsors might want to go beyond that and offer a retirement income menu. We have talked about the RMD plus the QDIA, but you could also do a systematic withdrawal plan with either a three percent, or four percent, or five percent payout rate and couple that with the QDIA.

That could be for people who want to customize their withdrawals. You could help enable setting up a retirement transition bucket by having a payout for a certain period. If you say, let me set aside money into the stable value fund and pay out $20,000 per year for five years, the plan sponsor could enable that by having certain period payouts. Finally, for plan sponsors who want to enable their employees to take more complex solutions but the plan sponsors do not want to offer them in their own plan, they can allow a withdrawal at age 59½. The employee could then roll his or her money into an IRA and then get more involved or complex retirement income solutions. This represents a very straightforward way that plan sponsors can change their 401(k) to many different retirement income strategies.

Key Takeaways for Older Workers and Retirees

The dilemma that many people are facing is limited retirement resources and the levers that they have to address their retirement situation are limited. They can work longer, or they can save more. However, once you are in your 60s, you are really not going to save your way out of a retirement shortfall. You can spend less in retirement.

You have got to stay healthy if you are going to work. You have got to make every dollar count. You really cannot afford a mistake or retirement income solutions that are inefficient. Key takeaways for older workers and retirees:

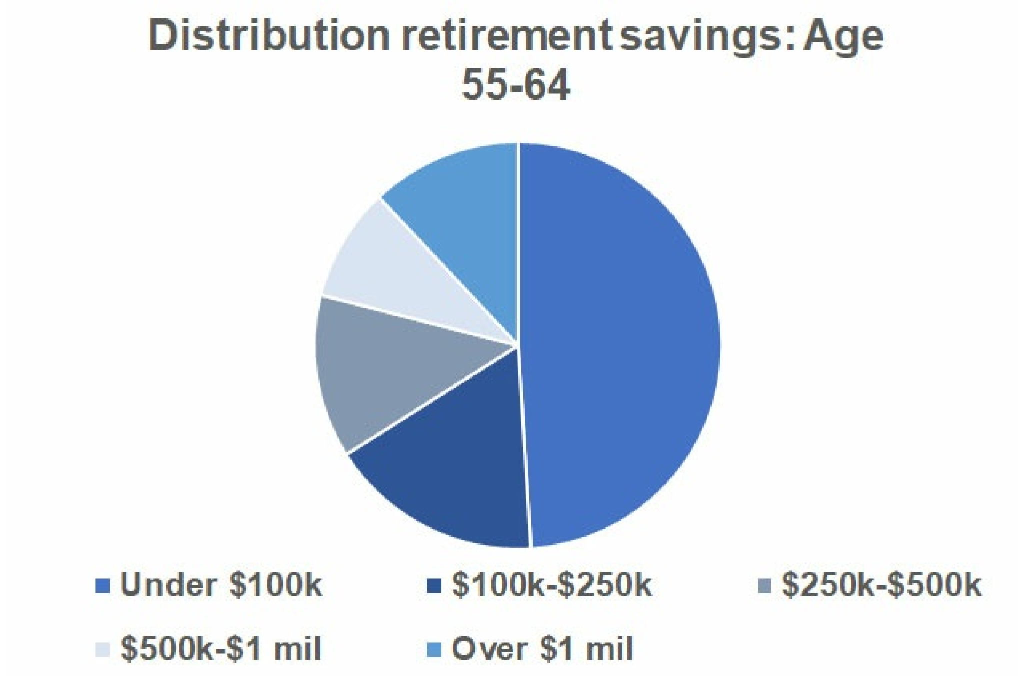
- It is smart to optimize Social Security through a thoughtful delay strategy.
- It is smart to automate the payment of retirement income so you minimize mistakes.
- It is smart to use low-cost index funds.
- For many people, it might be smart to phase into retirement for a period in your 60s until 70.
- It is also smart to adjust your withdrawals from savings to reflect your investment gains and losses so that if the stock market goes up you can increase your withdrawal and if the stock market goes down you decrease your withdrawal. That helps mitigate the sequence of return rate with which we are all familiar.
- Finally, it is smart to maintain some accessible savings. I think most people feel more comfortable knowing that they have savings that they can access.

For plan sponsors:

- It is smart to activate the RMD as the payment option on their plan.
- Offer period certain payouts to enable Social Security delay.
- Offer the RMD plus your QDIA as the default payout option.
- Offer low-cost payout funds — many plan sponsors are already doing that.
- Then provide educational tools and retirement income statements that we have talked about.
- Many plan sponsors are offering retirement planning assistance. I think that is an excellent thing.

However, let me add this last point. I think that as part of a retirement plan that a plan sponsor offers their older workers, part of that ought to be alternate career paths for their older workers, paths for them to downshift and not work quite as hard as they used to but still enable them to work and delay taking Social Security and delay drawing down their savings.

Let me just briefly go through the statistics that show levels of savings in America right now. This chart is just showing percentages of the RMD. That is just there to access if you want. However, this is the chart to which I wanted to get. This comes from the Employee Benefit Research Institute, the 2017 Retirement Confidence Survey. This is for workers age 55 to 64. On the right side, the blue side, almost half of workers have fewer than $100,000 in savings. They are the ones that I think are in trouble.

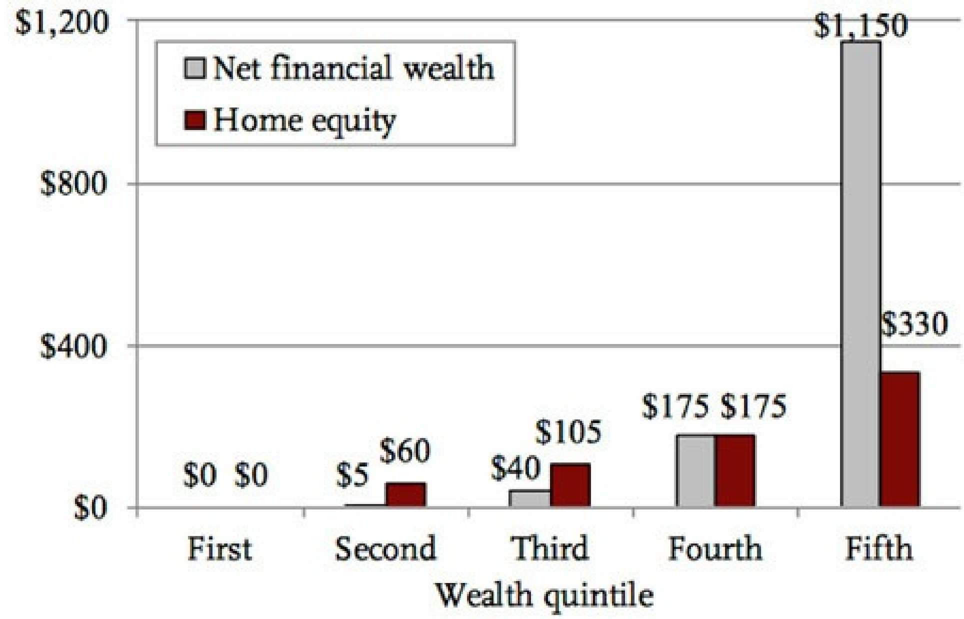


The lower left-hand corner is people who have between $200,000 and $500,000 in savings. They are going to need to plan very carefully.

Then the upper left-hand corner is workers who have between $500,000 and one million in savings and more than one million. They might have enough. This is just displaying what I was talking about earlier — that many workers are going to have to be very careful about how they transition into retirement. This is for workers age 55 to 64. There is a similar pattern for workers 65 and older.

This is a chart from the Boston College Center for Retirement Research showing different wealth quantiles for ages 65 to 69, and until you get to the fourth quintile, you do not have many savings. This is comparing home equity and financial wealth.

Figure 1. Median Home Equity and Financial Wealth of Households Ages 65-69 in 2012 by Wealth Quintile, Thousands of 2015 Dollars



This is displaying why many workers, particularly in the second, third, fourth wealth quintile, are going to need to explore how to use their home equity in retirement. As a result of these statistics, you see the different measures of retirement adequacy. Boston College is saying roughly half of households are at risk. EBRI is saying a little less than half are at risk. Fidelity is saying more than half of households are at risk.

There are various measures out there saying that many people are going to be struggling in the retirement years. I think it is up to the people in the room to help those workers. I am dedicating my life to helping these workers as well. Thank you for helping people with these challenges.

About Steve Vernon, F.S.A. – Expert in Strategies that Integrate DC Plans, Social Security, QLACs

Steve Vernon, FSA, is the President of Rest-of-Life Communications, and a member of the Executive Faculty and Research Fellow with the California Institute for Finance at California Lutheran University.

Steve Vernon shares practical strategies and ideas for enhancing finances, health, and lifestyle for the "rest-of-life" life phase, also known as retirement. With an effective mix of humor, stories, video clips, pictures, music, and cold hard actuarial analysis, Steve provides hope for working Americans with pervasive fear and anxiety about retirement. He is one of the most sought-after retirement experts in the country due to his surprising and inspiring insights. He is quoted frequently in such publications as The Wall Street Journal, New York Times, Los Angeles Times, USAToday, BusinessWeek, Fortune Magazine, Kiplinger's, and Money Magazine. He also writes occasional columns for Retirement Weekly.

How to "Pensionize" Any IRA or 401(k) Plan – Steve Vernon

Steve Vernon is active with research, writing, and speaking on the most challenging issues facing retirees today, including finance, health, and lifestyle. His clients at Rest-of-Life Communications have included AARP, Merrill Lynch, the International Foundation of Employee Benefit Plans, Weyerhaeuser, the Royal Bank of Canada, Sempra Energy, USC and Esterline Corporation. While at Watson Wyatt, his clients included Lockheed Martin, Northrop Grumman, Chevron, Unocal, Teledyne Technologies, Times Mirror, City of Los Angeles, H.F. Ahmanson & Company (Home Savings), Nordstrom and RAND Corporation.

He conducts research on behavioral finance at the California Institute for Finance at California Lutheran University. Steve recently headed a study sponsored by the Society of Actuaries on "The Next Evolution in Defined Contribution Plan Design: A Guide for DC Plan Sponsors to Implementing Retirement Income Programs in his position as a Research Scholar for the Stanford Center on Longevity.

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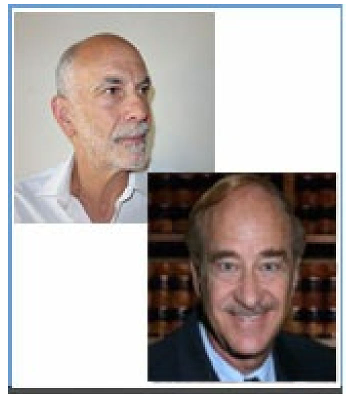
Integrating Home Equity and Retirement Savings Through the “Rule of 30”

By Peter Neuwirth, FSA, FCA, and Barry Sacks, PhD, JD

Up until 2012, many efforts had been focusing on ways either to boost the accumulation or to maximize the investment returns during the accumulation phase and even potentially after the drawdown period, but there has not been much attention spent on exactly how a retiree should be drawing down his or her income. Most retirement income strategies still consider withdrawals from the securities portfolio and maximizing Social Security benefits techniques (like saying you have to defer Social Security until the latest possible date and perhaps use your security portfolio to supplement your income until that point). However, very little in the way of sophistication was added to these kinds of strategies.



Peter Neuwirth and Barry Sacks

Editor’s note: This article is an adaptation of the live webinar delivered by Peter Neuwirth and Barry Sacks in 2018. Their comments have been edited for clarity and length.

You can read the summary article here as part of the 1st Qtr 2018 Retirement InSight and Trends Newsletter, worth 1.0 CE when read in its entirety (after passing the online quiz.)

You may also choose to take the full length course Integrating Home Equity and Retirement Savings Through the “Rule of 30” – Neuwirth and Sacks for 1.0 hours continuing education (CE)credit.

Now in the last few years, however, the industry has recognized that there are still a couple of issues that to be addressed. The first is that 401(k)s just are not going to do it. For most people their ending 401(k) balance, even when combined with other savings and Social Security, is just not going to be enough to provide an adequate level of retirement income. The second issue, and this is kind of the sleeper and the sneaky one, is that even with adequate savings, even if you have the amount that theoretically is enough to provide a retirement income, the investment volatility and sequence of returns risk, as well as the uncertain mortality, create a very significant risk for almost everybody that they are going to exhaust their assets before they die.

The answer to both problems (and this is now becoming more generally known) is that you just do not take from your portfolio when it is down because what happens is if you draw from your savings portfolio in a down market, you are doubling down on the exhaustion risk. At the same time, what we have found is that you can use home equity, which is that other big asset that most retirees have, to supplement your retirement incomes.

Four “Archetypical” Retirees

Until last year, home equity strategies were typically thought only to apply to what is called the mass affluent, the retirees with high savings and home equities. In 2017, we came to the idea that we could extend that idea and apply the strategy to a much broader class of retirees, so we did research to see if we could apply this strategy to four distinct kinds of retirees. *[Editor's note: Sacks' and Neuwirth's paper, "Integrating Home Equity and Retirement Savings through 'The Rule of 30'", was published in the Journal of Financial Planning, October, 2017.]*

We chose a large section of retirees that represented the wealthiest 50 percent of retirees because those are the people who have home equity. If you are below that level, you are just not going to have a home, and therefore, you are going to need to do something else.

What we also did was not just consider these retirees, but we also looked at different ratios of home equity to savings because the original study *("Reversing the Conventional Wisdom: Using Home Equity to Supplement Retirement Income", by Barry H. Sacks, J.D., Ph.D., and Stephen R. Sacks, Ph.D., Journal of Financial Planning, 2012)* only examined one class of retiree with one specific ratio. One of the key questions was, could we extend this strategy to classes of retirees that had different proportions of home equity and savings? It turns out the answer is yes.

We considered four different retirees. The first one (Retiree #1) which was the typical mass affluent retiree, is the kind of retiree that Sacks and Sacks addressed in their original paper. This is someone with a home equity of about $400,000 and retirement savings of $800,000. This is typical of somebody at the very top of the mass affluent, kind of between the 80th and 90th percentile of wealth in America.

While looking at the second kind of retiree (Retiree #2), we realized not everybody has that kind of balance between home equity and savings, so we consider it what we will call the "house-rich mass affluent". This is someone who might be living on either of the coasts and just has not been able to save as much in their retirement savings because they have been paying their big mortgage, but this is someone with home equity of $800,000 and retirement savings of $400,000. Again, this is more typical of mass affluent retirees on the East and West Coasts.

We then said there is a vast number of employees, multiple of many tens of millions of more retirees who are below that level, and the question is, could we extend this to that kind of retirees? We considered a third kind of retiree (Retiree #3), one we will call the almost affluent retiree, and this is someone who has far less in retirement savings and far less in home equity.

We assume they are kind of typical of the same ratio as was considered in the past of someone whose home equity was only half of that of their retirement savings. We assume this person has home equity of $150,000 and retirement savings of $300,000. This kind of retiree has never been considered before in the literature, but as we will see, this strategy that Sacks and Sack originally developed can be a very, very powerful strategy to use to enhance retirement income.

Finally, we considered the house-rich, almost-affluent retiree, and this is somebody who has the same total level of assets, $450,000, but two-thirds of those assets are tied up in home equity. This is the one kind of retiree (Retiree #4) who can benefit most dramatically from the use of a HECM (home equity conversion mortgage).

In 2012 when Barry and Stephen Sacks did their original study, it was a different economic environment, interest rates were somewhat higher, and the kind of common wisdom on unexpected returns was somewhat higher than it is today. What we chose to do for consistency's standpoint, just to make it more comparable to the prior study, was to use the same assumptions that were used in 2012 for this study. We did run sensitivity testing, which we will talk about. We will talk about how the results would change if you took a "more current view of the economy," but recognizing also, that the old assumptions were the kind of assumptions that were used to develop the four percent rule. In fact, if you use the current assumptions, you would not have a four percent rule to compare things to. You would have to use a three percent or a three-and-a-quarter percent rule.

The Analysis: Two Strategies Compared

We start by establishing a reverse mortgage credit line or a HECM, the home equity conversion mortgage, which is the most common, most prevalent sort of reverse mortgage.

In the first year of retirement, the retiree is to withdraw from the securities portfolio. In each subsequent year, we see how the investment portfolio performed in the preceding year. If it performed positively, then we will withdraw from it, and the reason is to harvest those winnings. However, if it performed negatively, we had a bad result and then did not choose to withdraw from the portfolio. Rather, we wanted to allow it to recover. Of course, any retiree has to eat, and one of the ways they can do it is to get some money from another source. That other source would be the home equity line of credit.

The actual analytic strategy involves adjusting the cash flow only for inflation. Whether the portfolio went up by little or a lot or not at all, you always drew the same amount as the preceding year, adjusted only for inflation. The purpose is to maintain constant purchasing power because most people whom we are considering, most of their spending is not discretionary, so it makes sense to think of needing constant purchasing power, even if the portfolio has gone down.

We call this the coordinated strategy — that is, we look at how it worked last year. If it went up last year, we draw from it. If it went down last year, we draw from the other source, namely the home equity credit line. I would call it the coordinated strategy in the original article, and we called it strategy number one in our more recent 2017 article. Pete gets the credit for wondering whether it could be used to apply to other ratios of home equity to retirement savings.

Remarkably, with a surprising consistency, the article we wrote initially in 2012 — and the article that Salter and Evensky and others wrote in 2012, Wade Pfau in 2016, Jerry Wagner in 2013 — all of them somehow looked at a ratio of 50 percent, 0.5 to one of home equity to retirement savings. Actually, when you think about it, more people have more home equity than they have retirement savings.

Let us look at the other strategy, the conventional strategy. In the conventional wisdom, the retiree withdraws only from the portfolio, unless and until it is exhausted, and only then establishes a reverse mortgage credit line and then withdraws from it. Now, why is that? Why is that the conventional wisdom? The reason is that it comes from an old idea that once the house is paid off, you should avoid incurring any debt that impacts cash flow. The unique thing about a reverse mortgage is that you do not have to make any payments as long as you continue to live in the house.

So how do we implement the model? The model is implemented using spreadsheet analysis with Monte Carlo simulation. What we are simulating is the performance of the securities portfolio and inflation. These two spreadsheets run side-by-side, simultaneously, where everything is identical, including the investment performance of the portfolio, the rate of inflation, and the amount drawn by the retiree (because that is always an initial amount subsequently increased only by inflation). It does not matter how the portfolio does regarding what is drawn.

The only difference between the two spreadsheets that are run simultaneously is the strategy for determining whether the retirement income was withdrawn from the portfolio or the credit line. That is where the Strategy Number One is used or Strategy Number Two is used.

What do we use as input parameters for this model? You start with the initial value of the portfolio, the initial value of the retiree's home, and the initial withdrawal rate. Consistent with the tradition of the four percent rule, it is what you stated as a percentage of the portfolio value, and the portfolio, which was assumed for both spreadsheets because they are identical, is a 60/40 stocks and bonds with annual rebalancing. We got data from various financial planners and investment managers that gave us the performance of those. In the 2012 article, we used historical data, which was fairly optimistic. In the 2017 paper, you will see results from both.

The focus of the analysis is on cash flow to the retiree, a constant purchasing power throughout a 30-year retirement. The Monte Carlo simulation runs 10,000 runs, and it runs a 30-year sequence of investment returns and withdrawals. Within a certain number of those repetitions, the cash flow is shown to survive for 30 years, and within others, it did not. For a given set of input parameters for each set, you will look at what the probability is: how many of those 30-year runs result in cash continuing to flow for all 30 years and if a set of parameters yields a 90 percent return. A 90 percent probability of cash flow survival — that is considered a successful set of parameters.

Obviously, if you put in a very low initial withdrawal rate, you are going to get a much higher probability of success, but the retiree will not enjoy his or her life as much. We are trying to find that sweet spot where the probability of cash flow survival is 90 percent, which means that it is as much as can be taken out to have that probability of enjoying life throughout a 30-year retirement. Anything less would be a higher probability of success but a poor lifestyle.

Key Findings

The first key finding is that Strategy Number One, the coordinated strategy, improves substantially over Strategy Number Two, with a far greater probability of cash flow survival. The second key finding was the interesting new result because the first one we found back in 2012.

For a particular initial withdrawal amount, as a fraction of total assets, if that results in a 90 percent probability of 30-year cash flow, then that same fraction of the total, that is home plus portfolio value, will result in a 90 percent probability of success across a broad range of both levels of total assets and ratios of home value to portfolio value, which is quite remarkable.

Total Assets	Initial Distribution (1/30)	Home value	Portfolio value	Survival Probability
$450,000	$15,000	$150,000	$300,000	90%
$450,000	$15,000	$300,000	$150,000	90%
$450,000	$15,000	$225,000	$225,000	90%

This would also be the case if total assets were $1.2 million and the withdrawal was $40,000 (i.e. 1/30 x $1.2 million)

Here is, then, an example to illustrate that. The total assets in this picture are $450,000. Look at the central column. Home value varies, and by extension, the portfolio value has to vary because the sum of the two has to add up to $450,000. To figure the initial distribution, use one-thirtieth of that total, and you will get $15,000, the same figure. Each of those and many more in between gives you a 90 percent survival probability.

That is what we found. That is the consistency across a range of ratios. Across a range of values, here is another example below, which says that this would be the same case if total assets, instead of being $450,000, were $1.2 million, and the withdrawal was, again, one-thirtieth. That is where we got the name, Rule of 30. One-thirtieth of 1.2 million gives you a $40,000 annual distribution adjusted for inflation with a 90 percent probability of that continuing for 30 years.

This is the key finding, and the safe withdrawal rate can always be determined as a fraction of the total home value plus portfolio value. When the investment returns used in the Monte Carlo simulation are consistent with historical averages, the fraction is one-thirtieth. That is how we gave it the name Rule of 30. Currently projected investment return figures, which are more conservative because of the markets, are over-inflated, so the future returns cannot be expected to be quite as favorable.

There was also a recent revision in the parameters applying to reverse mortgages. The result, instead of being a Rule of 30, is a “Rule of 38”. Nonetheless, whether you are using a Rule of 30 with historical investment returns and historical reverse mortgage parameters or current figures using a Rule of 38 instead, you nonetheless get a remarkable consistency across a range of ratios and a range of values.

Observations Regarding Cash Flow

The most important takeaway from here I think, as a practical matter and for the retirement income crisis in general, is that retirees with only modest retirement savings who own a home (Retiree #4) can dramatically increase the retirement income without risking the exhaustion of their resources by using this Rule of 30, as well, if they use Strategy One. If you look at what Retiree #4 can take using the four percent rule, it is peanuts— less than half of what he or she could take under the Rule of 30 and much, much safer.

Historically, financial planners have been telling people like Retiree #4 that they can only have a few thousand dollars since they only have $150,000 of savings. In fact, this retiree could have $15,000 in retirement income, which would make a huge difference in his or her lifestyle. Again, the total cash flow for retiree four throughout the entire 30-year period using this approach is actually even greater. It is 30 percent more total cash flow. The annual draw is much higher, and the total cash flow is also much higher under this.

Retiree	Home Value/ Portfolio/Total	Draw Using 4% Rule	Draw Using Rule of 30
#1	$400/800/1200k	$32,000	$40,000
#2	$800*/400/1200k	$16,000	$34,500
#3	$150/300/450k	$12,000	$15,000
#4	$300/150/450k	$6,000	$15,000

*Use $636,150 HECM

To put this in perspective, look at the last line in this chart. There are tens of millions of these retirees like this, and right now, financial planners are saying, if you are going to use a four percent rule, that may be too aggressive. Even so, you are telling people you can only take

$6,000 a year. In fact, if you combine it with a reverse HECM and you use the coordinated strategy, you could increase that initial draw to $15,000 a year, which could make the difference, a huge difference, to retirees at that level.

We mentioned before that the total cash flow available under this strategy is 29 percent higher than under the four percent rule. Part of that is because HUD FHA guarantees that even if the ultimate HECM loan balance exceeds the value of the home, the retiree nor his beneficiary will ever have to pay back more than the value of the home. Essentially, the government is providing a backstop in a very, very important retirement security guarantee through their program. They are getting plenty of premiums. That is what their insurance premiums, which are part of the upfront cost of getting a HECM, pay for.

This combination of Rule of 30 and strategy one provides this much higher cash flow without the risk of exhaustion than using strategy two for all retirees. It is both the mitigation of the risk of the adverse sequence of return and the impact of this HUD FHA guarantee. As described earlier, these results are remarkably robust across a variety of assumptions and for retirees with different levels of home equity and savings. In fact, everywhere from 50 percent, up to 200 percent ratio of home equity to retirement savings, the Rule of 30 works well.

Just last October, HUD (U. S. Department of Housing and Urban Development) changed the parameters under which future HECMs may be issued, and these changes include two different things. One is a new insurance premium structure and slightly lower, what are called PLFs, which are “principal limit factors”. The amount that is available under a reverse mortgage is slightly less than it used to be before this October 2017 change, so we built that into the calculations that led to the Rule of 38. The other thing that led to the Rule of 38, since the Rule of 30 was developed, was that interest rates and general expectations of future investment insurance had declined.

Let us leave out the HUD rules for a second. Without them, investment returns, which are lower, would say that if you are drawing from a portfolio, only then you should not draw more than 3.2 percent as the initial distribution amount. Thereafter, the same dollar amount is adjusted only for inflation. That is the kind of basic cash flow premise that is used in all of these analyses.

The bottom line in this is that the more house you have in proportion to the portfolio value at the outset, the more the house can do to continue the cash flow to buttress and offset those negative returns that occur, those adverse returns.

Key Takeaways

What we can make of this research and what kind of the exciting opportunities and necessary opportunities are there for additional research?

There is other good work that is being done by people like the Society of Actuaries and many other financial planners and researchers Wade Pfau and others addressing ways to address the expense side of the equation, the extent to which additional employment is necessary, ways of optimizing social security and so forth.

What our research shows is that there are vastly greater numbers of retirees than have previously been thought that can benefit from the use of HECMs — in particular, the use of HECMs with a coordinated drawdown strategy.

While results are robust and consistent across different economic environments and for retirees with different ratios of home equity/retirement savings, the INITIAL rate of withdrawal is sensitive to economic assumptions. For example, there is the strategy of saying, let us use the HECM as a last resort, but still, let us take it out initially as soon as you retire. It is kind of as soon as you retire, that would be a combination of the two.

There are approaches where you use the HECM for tenure payments. You turn it into an annuity, which has the advantage of being simple, but again, it is not as effective as this coordinated approach. There are other uses of HECMs that we are not addressing, such as the use of taking out a reverse mortgage and then using for long-term care insurance as a way of downsizing and paying off existing mortgages and various other strategies.

To some extent, this is really just the opening of the territory where there is an enormous amount of research still to be done and strategies to be mapped and discussed because different ways of using HECMs might be more appropriate depending on a particular retiree's situation.

One other thing became very apparent which was a little bit of a surprise to us as we pursued the research, was when we were looking at Retiree #4 in particular and realized just how critical those HUD FHA guarantees were to ensuring the long-term survival or protection against exhaustion of resources, we realized that this is a very important backstop to this strategy.

We think some additional analysis of these HUD guarantees need to be done. Preliminarily, we believe that it is not only an important government program, but it is actually well-funded via the premiums that are currently gathered. To some degree, HUD has been shooting in the dark and not knowing the level of premiums and the premium structure, whether or not it is going to be sufficient for the long term. I think that is manifested by the recent changes that HUD has implemented in these rules where the upfront premiums have been pretty significantly increased.

It is quite possible that there are going to be future changes in these rules, as well, and we need to be prepared for that. We need to be in close communication with the policymakers who are in charge of that. The bottom line is that it is not just the economic environment that is important, but it is also the HECM rules and the HUD themselves and how the lenders react to it. It is a dynamic, interactive situation, and as researchers and financial planners, we need to monitor, track it, and keep looking at it.

So, what are we leaving you with? What should you take away from this article?

Rule of 30 is a reasonable starting point for retirement income planning. When a retirement planner sits down with a new retiree or a future retiree, think in terms of the total assets, including home equity and retirement savings and think about the Rule of 30.

Think about the Rule of 38 depending on the investing environment or think about something in between.

Also, make sure you monitor the regulatory environment. It can change quickly. It can have an impact.

It is pretty clear that these HECMs, with their unique features, are worth utilizing and utilizing as soon as one qualifies. What history and research have shown is that taking out a HECM as soon as you retire is much more effective than waiting a long time.

About Peter Neuwirth, FSA, FCA

Peter Neuwirth is a Fellow of the Society of Actuaries, the highest designation they offered, a and Fellow of the Conference of Consulting Actuaries. He worked with WIllis Towers Watson for 38 years in both the insurance and the pensions world as a consulting actuary helping large companies manage their retirement programs. He is now retired and pursues freelance/independent projects that could benefit from actuarial thinking.

Integrating Home Equity and Retirement Savings Through the "Rule of 30" – Neuwirth and Sacks

In October, 2017, Peter Neuwirth, together with Barry and Stephen Sacks, published another article in the Journal of Financial Planning titled "Integrating Home Equity and Retirement Savings through the "Rule of 30"" which expands the prior research to the middle market from just the more affluent market, and the findings of which will be presented to you in this webinar.

Barry H. Sacks, PhD, JD

Barry Sacks, Ph.D. earned his Ph.D. in semi-conductor physics from M.I.T., and then taught at U.C. Berkeley. He earned a J.D. Harvard Law School, and is a Certified Specialist, Taxation Law, from the California Board of Legal Specialization. Barry spent 35 years as an ERISA attorney, specializing in qualified retirement plans. He then used his breadth of skills to discover a role for a reverse mortgage to help make a retirement portfolio last longer. Barry now has a law practice providing special services to tax professionals in the area of "Offers in Compromise" for retirees living on 401(k) accounts or other securities portfolios

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How to Protect an Aging Client's or Adult Child's Retirement Security from a Medical Crisis

retirement-insight.com/protect-aging-clients-adult-childs-retirement-security-medical-crisis/

By Annalee Kruger of CareRight Inc.

I used to be a social worker and long-term care administrator for over 20 years. Every day, I had families in my office because there was a medical crisis. Mom fell, she broke her hip. Hospital says here's a list of facilities. Go find one because we're discharging today at noon. The families are just completely caught off guard. They never thought about what is our actual plan if something happens to mom or dad? Who in the family is can drop what they're doing, leave work for a couple of weeks, and sort out what their options might be?

Rather than always being in crisis reaction mode, I started my company, Care Right Inc., with the mission of helping families be proactive and sitting down and talking about our aging plan sooner rather than later – ideally when things are still going well, because I've never had a family ever come back to me and say, "Gosh, Annalee, I feel really great. I'm really confident about the decisions that we had to make, when emotions were high, and time is limited."

Annalee Kruger, President, Care Right Inc.

Editor's note: This article is an adaptation of the live webinar delivered by Annalee Kruger in 2018. Her comments have been edited for clarity and length.

You can read the summary article here as part of the 1st Qtr 2018 Retirement InSight and Trends Newsletter, worth 1.0 CE when read in its entirety (after passing the online quiz.)

You may also choose to take the full length course How to Protect an Aging Client's or Adult Child's Retirement Security from a Medical Crisis – Annalee Kruger for 1.0 hours continuing education (CE)credit.

Why Have an Aging Plan?

It's about proactive planning. Just like you all help your clients plan, from a financial perspective, I help families plan from an aging perspective. Where is our loved one going to live? How is care going to get paid? Who is going to provide that care? One of the main advantages of having a neutral third-party person facilitate these family conversations is because these are sensitive conversations to have whether we're talking about incontinence or memory issues or family dynamics and family dysfunction. People need a trained, neutral, third party person to really navigate these kinds of conversations because most families when they call me are already so strained with their relationships with their siblings and with their parents.

Where is the loved one going to live? Who will provide that care? And how will care get paid? Most of my calls are from an adult daughter who is the primary caregiver. She is also taking care of up to six other aging parents or six other aging loved ones, whether it's her parents and step parents, and then her in-laws, which she may or may not like. She might also have that stray aunt or uncle who outlived their children or never got married. It's a very good conversation starter to help these families communicate about what they have in place and what more do they need to put into place.

Another advantage of proactive planning is because, when you get older, your conditions can change very quickly. No one ever expects or plans to have a stroke. No one expects to fall and hit their head and have a subdural hematoma that's going to be life changing. No one ever plans for these things, and yet they happen every day. You don't want to be willy nilly about your care and your aging process. When you're the most vulnerable and the most dependent, you really need to make sure that you have a plan, otherwise, you're going to likely get sub quality care by sub quality care providers.

Many facilities such as assisted living, memory care units, or nursing homes, have long waiting lists. You must financially qualify (a lot of people don't know that) so they're waiting until the last minute. These are important things to address with clients because people don't know what they don't know so then they make expensive decisions and mistakes.

You must plan for where are they going to get their care and making sure that they qualify for places to be able to move into. There are significant cost savings when you plan ahead. In 2015, there was a study by Genworth that outlined that caregivers estimate that proper planning would have resulted in, basically, saving them about $8,000 in out of pocket expenses.

Last year, I had my clients, my primary caregivers who were the ones that were kind of the go to person for the family, kind of calculate how much money they spent out of pocket for their aging parents' needs just in travel expense. Daughters and sons were spending an average of $18,000 out of pocket when they had more than one person that they were tending to that's elderly because, again, if you must fly to wherever that loved one is when you get that crisis call, air fare is not $200. You rent cars, rent a hotel room. It's very expensive. When you have more than one person you're taking care of, it's a lot of out of pocket because, again, families don't have a plan in place.

This doesn't count the time away from work. If they're an employee, they're losing income. If they're a business owner like me, they're losing out on revenue because they must tend to the needs of their parents. A lot of my clients are business owners. They are very busy. They're realtors. They can't make money if they're not in their area to make money. If they're in Colorado, instead of down here in Florida trying to sell houses, you can't do that when you're in Colorado.

What is a Family Caregiver?

A family caregiver is a spouse, adult, child, or other relative, partner, or friend who has a personal relationship with and providers a broad range of unpaid assistance for an older adult with chronic or disabling condition. Dementia, aging, multiple sclerosis, ALS, any of those kinds of chronic conditions. What's key there is it's unpaid. Some are quitting work or taking early retirement so that they can have the flexibility in their schedule to take care of their aging parent. Families financially jeopardize themselves so that they can be available and provide the hands-on care and supervision that their loved ones need.

- The typical caregiver is usually female – it's usually a wife, a daughter, or daughter-in-law.
- 52 percent of these caregivers are adult children taking care of their parents.
- 60 percent of the caregivers are between the age of 25 and 54.
- The average caregiver age decreased from age 53 in 2010 to age 46 in 2015.
- Over two-thirds of caregivers sustained their commitment for more than one year; a third of them for over five years for one person.
- Caregivers miss an average of seven hours per week of work or 18 percent of a 40-hour work week. When you look at 33 percent of the average income is lost by caregivers each year because of their duties of being a caregiver. In 2010, 64 percent of caregivers missed work due to caregiving. In 2015, 77 percent of caregivers missed work due to caregiving.
- Often, caregiving leads to retiring early. They decline their job promotions. They take menial positions because they need the flexibility in their schedule. And they're also quitting their jobs to move closer to their aging parent. This is something that I hear every single day from my families that I meet with.
- In 2010, only 41 percent of the caregivers were funding their aging parents. In 2015, 62 percent of their parents were being funded by their adult children.

Caregivers sometimes fund their aging parents because they don't know their parents already have long term care insurance. Everybody seems to think that Medicare is one of the retirement buckets that they can count on. However, Medicare does not pay for things that everybody seems to think that it will.

The Health of a Family Caregiver

When you look at the health perspective of being a family caregiver, 54 percent of caregivers experience negative feelings, including guilt and resentment. Forty-three percent of caregivers said a long-term event negatively affected their personal health and wellbeing.

In the beginning, it starts out, "I can help you with your mail. I can bring over some milk. I can do this, I can do that". The next thing you know, they're taking time off work, and they're not taking vacations, they have no vacation days left because they've had to take their parents to the doctor's office. Oftentimes, they've already exhausted their FMLA benefit.

People with Alzheimer's disease require an average of 70 hours per week of supervision and care. Sixty-two percent of those hours are usually provided by a family caregiver.

Approximately 80 percent of dementia patients are cared for at home by their family members. Most caregivers report feelings of anxiety and depression. Probably four times a week I get calls from adult children who say “I’m on medications for anxiety, depression. I’m not sleeping at night. My family doesn’t even want to hang out with me anymore because I’m just moody all of the time.”

About 70 percent of people turning 65 can expect to need some form of long term care during their remaining lives; that’s why it’s so important to have these conversations. I don’t care if you’re 80 years old or if you’re 50 years old or 30 years old. These are conversations that families should have because you never know what’s in store for you every day. Why does this matter? Because there’s a family caregiving crisis epidemic out there. We all have heard about the opiate epidemic. And there is, for sure, that. There’s no question about that. But I am telling you, with almost a 30-year career, there is a family caregiving crisis out there that no one is talking about.

Family caregivers are in survival mode. They’re trying to make it through their day, but it’s at the expense of their own wellbeing. I just wrote a book about the portrait of a family caregiver. It’s called, “*The Invisible Patient.”* Everyone always asks how dad is doing. Well, dad is doing fine, but it’s because I’m missing work. It’s because I’m missing time away from my family. It’s because I am his assisted living. They’re just in survival mode trying to balance their work, their own family, their career, and not feel guilty about not being available as much as their parents might need.

Caregiving for Ethel and Marvin

It’s Ethel and Marvin’s second marriage. They both have three children, so six kids live in six different states. Ethel has memory impairment. Marvin is her primary caregiver.

Six children live in six different states. How well do the kids and step kids all get along? What is Ethel and Marvin’s relationship with their adult children? What’s the relationship with the children and their respective step parent? We know dementia is a progressive disease. We know that Ethel will need more and more care and oversight as her disease progresses. We know that Marvin is her primary caregiver who is also up in years. Most likely, he’ll be having his own physical health issues.

Yet he’s also needing to tend to Ethel because, at some point, Ethel won’t be able to stay home by herself and at some point, Ethel will need supervision 24 hours a day. She’ll need help with bathing, dressing, grooming, giving her her medication. So, that’s what a typical picture will look like, if you’ve got clients with memory impairment.

They’re not easy slam dunks, when you’re dealing with second marriages or second relationships or families that don’t get along and then they live remotely from each other. For complicated situations it is critical that they have these conversations as a family and a plan put together by a neutral third-party person. Do you think it would be wise to understand the liability issues involving the memory impairment, from your perspective, from being an advisor?

An advisor in Wisconsin attended a workshop that stated families are starting to sue advisors because they're like, "Of course Mom has memory impairment. How can you not know that?" So as an advisor, it is essential that you learn about memory impairment and what are the red flags, and how does that affect you and your business and your livelihood, and those assets under management because what do you think will happen to the assets under management when either Ethel or Marvin dies?

Final Thoughts and Takeaways

- There is an opportunity cost of not addressing aging and family caregiving issues with your clients. Poor planning or no planning results in increased care cost, hence lower assets under management.
- It is important to put a plan together. One of the things I have learned with working with advisors these last few years is that most advisors that I've met anyway through sponsoring Financial Planning Association (FPA) chapters and speaking at the annual FPA Retreat don't really understand the aging process. Why would you? How would you know unless you've worked in long term care?
- There's a real opportunity to learn about the aging process and really what it's like to be a family caregiver. If you have clients in that role it's critical for you to be a resource for them. Let them know that even thought this isn't in the scope of your practice, there are people who can help them develop a plan, so they don't get burned out, so they don't have to use up all their vacation days tending to aging parents. Developing deeper relationships with your clients and their adult children is going to be essential.
- Develop your team of trusted professionals that make you look good. Refer your clients to professionals who can meet their other needs. If you meet your clients' holistic needs, they'll refer you to friends and families.

About Annalee Kruger, President, Care Right Inc.
Annalee Kruger's mission is to help families be pro-active and put plans in place before a medical crisis occurs. While she serves families in SW Florida, she also serves families across the US. Gone are the days of families living in the same zip code, let alone time zone. Annalee helps families with her virtual guidance service and virtual family meetings and family coaching/education.

How to Protect an Aging Client's or Adult Child's Retirement Security from a Medical Crisis – Annalee Kruger

In 2011 she founded Care Right Inc. to help families with aging loved ones navigate through the long-term care industry and cope with issues family caregivers encounter. Care Right's mission

is to help families be pro-active by facilitating
difficult conversations early on, explain the importance of having their legal documents in order, explain the costs of health care, why having a financial plan is important, and developing a plan of care which incorporates the legal and financial planning.

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