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Bonds Away! How Fixed Income Can Play an Integral Role in Any Retirement Strategy

Russell Wild, MBA, Principal of Global Portfolios

Editor's note: This article is an adaptation of the live webinar delivered by Russell Wild in 2023. His comments have been edited for clarity and length.

You can read the summary article here as part of the April 2023 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 Bonds Away! How Fixed Income Can Play an Integral Role in Any Retirement Strategy for 1.0 hour continuing education (CE) credit.

By Russell Wild, MBA, Principal of Global Portfolios

Welcome to the wonderful and wacky world of bonds. Why wacky? Almost nothing I can think of, not even writing a novel, that looks so simple but can be so complex once you delve into it. If you have ever been lost in some complexities, we can clear some of that up today. Today we are going to look at the significant role bonds play or should play in building a retirement portfolio. We will examine what kinds of bonds belong and which do not belong in retirees' accounts. We are going to take a look at bond funds, individual bonds, and bond ladders, and we are going to look at the risks of bonds. Finally, I will give you some tips for successful bond trading.

The History of Bonds

When I did my first edition of *Bond Investing for Dummies*, I relayed a story from a wonderful book called *The History of Interest Rates*, published by Wiley St. Publishers, telling the story of how one man lent a half mina of silver to another. In the presence of a holy priest and four fellow citizens, it was agreed that within one year, the lendee would pay back the half mina of silver along with ten shackles. Each shackle was worth 1/60th of a pound of more or less silver; if you do the math, the interest rate was 33 and a third percent. This transaction was very similar to a bond transaction today. There was an issuer, a lender, a borrower, a contract, and interest. As I said, it all seems very simple.

Let us go back even 1,015 hundred years more to the second millennium BC. We are now in ancient Mesopotamia, and gold and silver coins did not yet exist. If any of you read Cuneiform, you basically see a contract on a tablet. You may notice a buyer, a borrower, a lender, and what looks like some grain passing hands. If we go back then 2,700 years, there were, in effect, bond dealings, or simply, an "I owe you." Since they did not have silver coins, they used cows or sheep to transact business, perhaps enslaved people, but most commonly, grain.

As the years went on, bonds developed into certificate form. Let us move forward to the 1100s in Venice. Venice is at war with other city-states on the Italian peninsula. Venice needed money to raise for waging war. It turned to its citizens; those were the first real modern bonds. They offered what was called a prestito at a fixed interest rate. The interest rate decreased from about 33 percent to 12 or 15% in those days. A prestito, by the way, was like today's bonds, but they were infinite. There was no maturity date. So, if you held a prestito, you would earn 12-15% every year for as long as you held it, which would be the rest of your life, unless you sold it.

Bonds were eventually issued with actual coupons, and they were ripped off or cut out and turned to the borrower, who would then pay you back what was then called and still called the coupon rate. So, if you had a $1,000 bond earning five percent, you would get $50 a year for as long as you held the bond or until the bond's maturity. It still is called a coupon.

In 1982, the US government decided that too many of these bonds, called bearer bonds, were allowing the holders to hide their interest collected from the taxman, so just about all bonds went electronic. So, now the US Treasury issues a statement indicating that the holder has holdings in US Treasury bonds. Currently, bonds are held by banks and brokerage houses, or you can get them directly through the Treasury. All you will have is an electronic statement, just as you do with stocks, which no longer issue certificates. The only exception I know of is the US Treasury, which still offers some savings bonds in certificate form, which you can buy with a tax refund of up to $5,000 a year.

Why Invest in Bonds?

Depending on your age, your grandparents or perhaps your great-grandparents may have been saved from destitution or from having to sell apples on the street during the Great Depression because of bonds. In 1929, the market lost about 12-13% on Black Monday, and the same thing happened the next day. Over the ensuing weeks, it lost another 25%; in the end, the Dow lost 90%. It would come back until the Japanese attacked Pearl Harbor in 1941, and we entered into a wartime economy.

It was a long, dragged-out, severe depression, but bondholders did rather well. Over that decade or so, bonds never lost value. US Treasuries earned about six percent a year, and remember: this was not a time of inflation; this was deflation. So, prices were going down, and six percent was a very handsome take for bondholders.

Why hold bonds? Because bonds pay cash. Every month, every three months, every six months, you will get, again, a coupon payment which is cold, hard cash. I cannot think of many other investments that promise you a steady stream of income.

Why hold bonds? Because even if we are not headed toward another depression, many people have a hard time with the daily ups and downs of the stock market. Bonds tend to smooth out a 60/40 portfolio. Bonds and stocks, stocks and bonds will be much less volatile than a portfolio of all stocks. Bonds have a zero correlation with the stock market. If the stock market goes down, sometimes the bond market will go down, but there is no reason for it to. It may go up when things get rough. The safest bonds, Treasuries, especially long-term Treasuries, do tend to go up. There are no better hedges than bonds.

Cash is the second-best hedge after bonds. The problem with cash, of course, is if you put money under your mattress, you are going to lose two, three, or four percent a year, whatever the inflation rate is. And even if you have your cash in a money market or savings account, you will still be lucky to keep up with inflation.

Gold is an excellent diversifier when it wants to be. Sometimes it moves in lockstep with the market; sometimes, it moves against the stock market. It is always very volatile, and of late, because gold has become very liquid with the coming of all kinds of gold ETFs, we are finding more correlation with gold than we have in the past. Gold has a long history of almost keeping up with inflation.

Then there are REITs, real estate investment trusts, and high dividend-paying stocks, which have limited correlation to bonds but are correlated to the stock market. They will tend to go down when the stock market goes down and up when it goes up. For that reason, they are not great hedges, and dividends are different from interest payments, and dividends are not guaranteed.

There have been index funds and mutual funds for years. Lately, there have been dozens and dozens of inverse ETFs introduced to the market, whereby if the S&P goes down by five percent on a particular day, your inverse ETF will go up five percent. A perfect negative correlation is a great hedge. These funds tend to be pretty pricey, and you are fighting a juggernaut. The stock market goes up over time. And for that reason, people have lost money on these inverse funds over the years.

Not all hedges are created equal. And if we look back over the last 50 years, stocks have returned to a healthy 10% a year. The three-year standard deviation of the S&P 500 is 21.1 percent, which is very volatile. Bonds have earned about half as much, with much, much less volatility. Gold has returned not half of what bonds have returned, and cash has just about kept even with inflation.

What Kind of Bonds Belong in Retirees' Portfolios?

When I have been talking about bonds, I have been talking about investment-grade bonds. These bonds have minimal credit risk, and there is minimal risk or no risk that the issuer will go bankrupt.

There is no risk with Treasuries and minimal risk with companies like Microsoft and Apple. I suggest that retirees' portfolios should be bond portfolios and all investment-grade. High-yield junk bonds over history tend to return about two and a half to three percent more a year than investment grade. But they can be very volatile and correlate to the stock market. When we go into a recession or a depression, companies fold. And those companies will no longer pay bond interest or the principal. So, high-yield junk bonds are risky. I am not saying there is never a point in owning them. But investment-grade bonds are part of a retiree's portfolio that serves as ballast and as a hedge.

Once we decide we want a portfolio of investment-grade bonds, the next big decision is government versus corporate. Government bonds, or US Treasury bonds, were considered the safest because if the government can tax, presumably, they will never go bankrupt. And if it does, we are all in much trouble. Government bonds pay about a point and a half less than investment-grade corporate bonds over history.

Muni bonds can be a very good substitute for corporate bonds. Muni bonds belong in your clients' portfolios in the stratospheric tax brackets. To estimate the taxable equivalent yield of a muni bond, you start with a straightforward formula. Take the muni bond yield and divide it by the reciprocal of your marginal tax rate. So, if a muni bond is paying five percent and you are in a 30% tax bracket, you divide the reciprocal of that or 70 into five percent. A muni bond paying five percent would have a tax equivalent yield of about seven percent.

The next big question is whether you want short-term, intermediate-term, or long-term bonds or a little of each. Short-term bonds tend to be much less volatile 90-95% of the time under normal conditions when the yield curve increases. When the yield curve increases, short-term bonds will be less volatile but pay less, and longer-term bonds will tend to yield more.

The Risks of Bonds

We talked earlier about credit risk. People first think of this when they think of risk in bonds or the risk that the borrower will go bankrupt. However, a borrower does not have to go bankrupt for you to lose money. There is also downgrade risk. When a bond goes from investment grade to junk or from triple A to double A or AA to A, you are taking on downgrade risk. I looked a couple of weeks ago at Bed Bath & Beyond bonds. At the time of this writing, their bonds yield 40%, and there is a good chance that you will not get your money back since they've been downgraded. The price of Bed Bath & Beyond bonds has significantly fallen.

Downgrade risk and credit risk are, again, what people think of most. But a more considerable risk in my mind, as we saw over the last year, is interest rate risk. The price of bonds moves inversely to interest rates. So, bond prices went down when interest rates went up as they did in 2022.

Reinvestment risk is the flip side of interest rate risk. With interest rate risk, you are afraid interest rates will go up, pushing your bond prices down. With reinvestment risk, you are afraid that interest rates will go down if you have too much in the way of short-term bonds. Remember, you are getting that fifth on a five percent, $1,000 bond. You are getting $50 a year for the 15-20 years you hold that bond. Reinvestment risk means you cannot reinvest that $50 at the same rate.

Bonds have just about kept even with inflation over the last 50 years. Aside from last year, it has been a good time for bonds. We went from the very high-interest rates of the 1980s when bonds were paying double digits 15, 16, or even 17% quality bonds down to the beginning of last year when Treasuries were paying about zero. So, even now, bonds just about kept up with inflation. There have been other times throughout history when bonds have not done a good job of keeping up with inflation.

Finally, there is FOMO or fear-of-missing-out risk. I have seen people come to me who really should have more conservative portfolios than they do, which is to save more bonds than stocks. But if the market is doing well, they see their neighbors, their friends, their hairdresser, and their plumber talking about how much they are making in the stock market. That can depress some people.

What Happened to Bonds in 2022?

Because of rising interest rates in 2022, the aggregate bond market lost 13.2%. When I talk about the aggregate bond market, that is the world of investment-grade taxable bonds, or two-thirds Treasuries and one-third corporate.

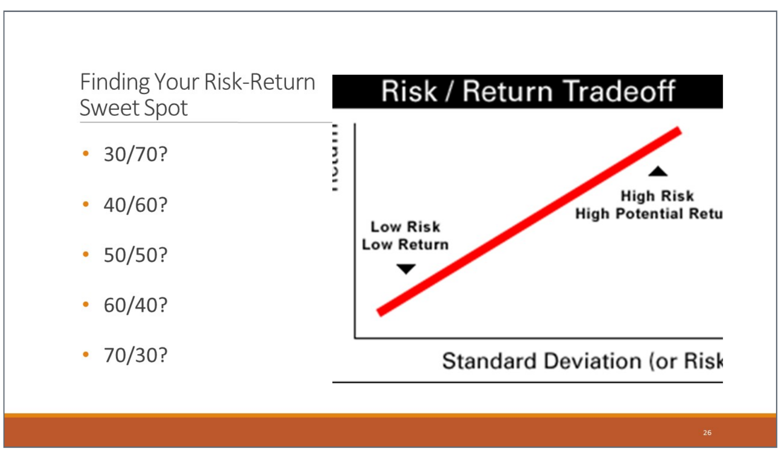
2022 was the worst year for bonds in history ever. Why? Let us go back to early 2020, in March- April. We had never heard of COVID before. And suddenly, we see an epidemic that turns into a pandemic. People are not going to restaurants, not going to bars, not going to stores. They may not be going to work. They may not have work to go to. We start spiraling into a recession, perhaps a depression. And the government responds to this the way, not only our government but most governments worldwide; certainly, all Western governments respond the way governments usually respond when they fear a coming recession or depression: they lowered interest rates. They lowered them and lowered them and lowered them to the point that Treasuries were paying about zero. German and Japanese sovereign bonds went below zero and were paying negative interest rates.

A year or two years go on. Most people get vaccinated and realize that if they catch COVID, they will probably not die; they will probably have flu-like symptoms. When I had COVID, it was not even that.

As the economy started kicking up again about a year ago, Russia invaded Ukraine. Suddenly, supply chains freeze up, especially oil. The rising price of oil, the closing of supply lines, people rushing back to fill their consumer needs that have yet to be filled, and suddenly we start seeing high inflation as high we have not seen since the 1980s. Governments respond the way they usually respond to inflation fears – they start raising interest rates. They raise interest rates and raise interest rates and raise interest rates. Until today, the 10-year Treasury is paying about four percent. Because we have an inverse yield curve now, shorter-term Treasuries are paying about five percent.

So, percentage-wise, that was a massive hike. We saw a perfect storm. Again, as interest rates go up, bond prices go down. The chances of us having another year like 2022, I will not say is impossible, but pretty close to it. Now if I can ballyhoo bonds once again as something that belongs in most retirees' portfolios, if not all, keep in mind 2022's 13.2% loss. Several times over history, the stock market has lost almost as much or as much in a single day. And last year, the S&P lost about 20%, and the NASDAQ about 33%. So, even in the worst year for bonds ever, bonds still served as a decent hedge, still served to smooth out volatility in seniors' portfolios.

What percent of my retirement portfolio should be in bonds? There are all kinds of formulas. I am not going to discuss it in depth because other speakers talk about this in great depth and do a very good job of doing it. I will say that many, many studies look at safe withdrawal rates. The safety of portfolios suggests that most peoples and most retirees' portfolios should be somewhere in the range below:



A very not risky 30% stock, 70% bonds would be a mild non-aggressive portfolio compared to a 70% stock, 30% bonds portfolio. Most retirees should be somewhere in the middle, somewhere between 40 to 60% stock and the rest in bonds.

How to Choose Bond Investments?

We've addressed the broad questions to ask before getting into bond investing. Now let us look at some of the particulars, nuts, and bolts.

You can invest in individual bonds, or you can invest in bond funds. I favor bond funds for several reasons. Bond funds have decreased in price remarkably over the last ten years, and trading individual bonds has not changed much. Bond trading and bond funds can be very economical, and bond funds also allow for easier diversification.

They also allow for automatic reinvestment, which individual bonds generally do not, reducing cash drag. If you are going to go with funds, I urge you to keep costs low. That is even more important with stocks than it is with bonds than it is with stocks because you are looking at a lower return. So, costs can eat up a much greater percentage of that return.

As we talked about earlier, do stick with investment grade. If you have a small portfolio, look at a broad core bond fund that invests in Treasuries and corporates with a larger portfolio. You may want munis in your taxable accounts and corporate bonds in your retirement accounts. Diversify. Diversify. Although funds do a great job diversifying within an asset class such as corporate bonds, you may want to have several kinds of bond funds, such as Treasuries, corporate, agency, and municipal.

Study after study shows that buy-and-hold investors do better than those who frequently trade because there are all kinds of trading costs when you trade that are often unseen.

How low can you go with bond funds? Fidelity, Vanguard, BlackRock, the bond funds, plain vanilla bond funds, where we are talking three, four basis points. For example, the PNY Mellon Corp bond fund has an expense ratio of zero.

Consider ESG bonds. ESG stands for environment, social, and governance, which used to be called corporate responsible or sustainable bonds. You should align your values with your investments, and ESG is just another tool that can be used to look for risks. You may not want to invest in corporations with lots to lose if there is continued coastal flooding. One study by New York University and Rockefeller Asset Management looked at 1,141 other studies, including other meta-studies. They found that the great majority of companies that score high on sustainability tend to be more profitable, and their investors tend to get greater returns.

Now, moving to individual bonds. If you are going to invest in individual bonds, and there is no reason you should not invest in Treasuries, if you want to, you can get a Treasury refund bond for almost nothing. But if you want to invest with Treasuries, especially directly through Treasurydirect.gov or through a brokerage house, I know Fidelity and Vanguard do not charge anything for Treasury trades. Go ahead and do so.

But where corporate bonds and munis are considered where you are going to pay for trades, and you need diversification, I suggest funds. But if you want to go with individual bonds, please make sure you use TRACE or urge anyone you know to use TRACE. TRACE is FINRA's system of tracking bond buys and sells. TRACE has been around since 2002, yet many people still trade bonds without looking at TRACE. TRACE is now available through most large brokerage houses. You can see where a bond was last traded. If it is a frequently traded bond, maybe minutes ago, you will see the price that it was traded for or the price it was purchased for. You will know exactly how much the middlemen are taking.

Plan to hold bonds to maturity if you buy individual bonds. That way, you are only dealing with the expense of one trade, not two. And ladder wisely. Do not be a slave to the yield curve. Let me explain what I mean by that. Laddering, of course, is having short-term, intermediate, and long-term bonds. This is especially important if you invest in individual bonds for a retiree who needs cash. You want bonds coming due to provide that cash over however many years. Do not be a slave to the yield curve. Right now, we have a very unusual downward-sloping yield curve, maybe less than 10% of the time; we do not have an upward-sloping yield curve. So, it means that you can buy long-term bonds, which are more volatile and get less return than you earn on short-term bonds.

Why would anyone want to have long-term bonds? Again, remember reinvestment risk. So, right now, you can get about five percent on a one-year Treasury and four percent more or less on a 10-year Treasury. If you have all one-year Treasuries, what happens in a year if interest rates start tumbling again? What are you going to do with all the proceeds that you are going to be collecting in one year? You are not going to be able to reinvest them. Not even at four percent. Perhaps you will not even get one percent. So, that is why it makes sense, even in times like this with an inverted yield curve, to have some intermediate and long-term bonds.

What do you do once you have bonds in your portfolio? Many people like bonds because they are a steady stream of cash, which is true. In the old days, retirees with bonds in their portfolios lived on their bond interest. The problem is that bonds tend to just keep up with inflation, maybe do a little better. If you take the interest out of the bond side of the portfolio, the bond side will shrink, and you want to keep your portfolio in proper alignment. At the same time, buying low and selling high is always great. So, set your bonds to reinvest automatically, reduce cash drag, and rebalance every six months, every nine months, and every year. If stocks have had a wonderful six months, you sell stocks. If bonds have had a wonderful six months and stocks have shrunk, you sell bonds. That way, you are constantly buying low and selling high and can juice your returns over the long run. More importantly, though, you will keep your portfolio in proper alignment.

Very Common Bond Myths

I want to talk about a few very common bond myths.

First bond myth: You can buy a bond at a discount, or you can buy a bond at a premium. It sounds better to buy a bond at a discount, but it is not. If you buy a bond at a discount, such as a Bed Bath & Beyond bond, there is a reason you are getting it at a discount. You are getting a discount because it used to be a AAA bond, and now it is a BB bond, or you are getting at a discount because it is paying $50 a year.

Interest rates for bonds have gone up. Bonds issed at a 5 percent coupon now need to yield seven or eight percent. So, a bond paying $50 a year instead of $70 a year will sell at a discount.

But discount bonds and premium bonds will tend to have the same yield. Premium bonds are probably paying more, which is why they are premium bonds. They were issued at a time when interest rates were higher. Let me say that discount bonds can actually wind up smacking you more tax-wise because if you buy a bond at a discount, you buy a bond that is, say, $900, and then sell it at a $1,000 two years later, you are going to pay a capital gain. And that holds even if it is a muni bond.

Second bond myth: A bond paying X percent today will pocket you X percent over the bond's life. As you will recall, I said bonds look very simple but can be very complex. A 20-year bond that you buy at five percent will not necessarily earn you 20% over those 20 years because there is a reinvestment factor. Your bond will pay $50 a year, and you need to reinvest that. You do not know if interest rates are going up or down. Even though bonds are a lot more predictable than stocks, they are not entirely predictable.

Third bond myth: Rising interest rates are good. Sometimes you will hear they are bad for bondholders. Certainly, right now they are because people's bond portfolios have lost 13% over the last year, although they have made something of a comeback in the last two months. You are hearing that rising interest rates are bad for bondholders. Keep in mind that you are currently getting healthy interest on your bond portfolio. Those Treasuries you may be holding are paying four or five percent right now, whereas a little over a year ago, you would have been getting zero. Over the very long run, rising interest rates are probably good for bond investors.

Fourth bond myth: Certain bonds, such as Treasuries, are completely safe. Treasuries presumably are free of credit risk, but they are certainly not free from reinvestment risk or interest rate risk. As a matter of fact, long-term Treasuries tend to be particularly sensitive to interest rates. So, we can see big swings in the price of Treasuries. Even though they are sometimes called completely safe bonds, they are not.

Fifth bond myth: Bonds are a retiree's only true friend. I love bonds, and I hope I have conveyed that to you. But bonds are not a retiree's only true friend. If you have a portfolio of all bonds, you are going to have to spend very modestly in retirement because your portfolio is probably going to just keep even or maybe a little better with inflation. So, a retiree's true friend is a diversified portfolio that holds bonds.

Sixth bond myth: My favorite myth is that I do not have to worry about interest rates because I will buy a five percent bond for 20 years. I know exactly what I am getting and can laugh off interest rate movements. Let those people with bond mutual funds sweat it out. I am going to sleep well. Let's look at Big Joe, who buys himself an individual five percent bond, say a Treasury bond, with no credit risk. He is going to hold it for 20 years.

Little Joe buys a bond mutual fund, and his mutual fund will see many, many ups and downs over the coming years. Well, let us say interest rates go up. Little Joe will not be getting five percent; he will get six, seven, or eight percent on his bond portfolio. And Big Joe will be eating crow for 20 years, earning five percent, but he is not taking any interest rate risk. No, I am afraid there is no way to avoid interest rate risk.

Key Takeaways About Bonds for Retirees

I hope I have communicated that investment-grade bonds lend crucial stability to a retirees' portfolio and, for that reason, belong in all retirees' portfolios.

Let me say bonds are the most common form of fixed income right now. And at certain times, CDs pay as much or more than bonds. So, CDs can be a good substitute.

And in certain circumstances, a fixed annuity can also fill that role. But for most retirees' portfolios, a good chunk of investment-grade bonds makes all the sense in the world.

I hope I have impressed you also that 2022 is considered a black swan event with a fat tail, and it was the perfect storm and will not happen again anytime soon. As I have shown you, even though bonds had the worst year in history, it still serves as a decent hedge for retirees.

Fixed-income portfolios should make up 50 to 60% of most retirement portfolios. Again, this is based on many studies that show that to have a portfolio that will keep up with inflation but not be too much at risk from the volatility of markets, you want something in this ballpark.

As we covered at the end, you want to sell high and buy low by rebalancing stocks and bonds. Do not just have the bond portfolio and take the cash out of it to pay for the bills will lead to an uneven, unbalanced portfolio.

And finally, especially because bonds do not return what stocks return, you want to keep your costs very low and trade at a minimum.

Bonds Away! How Fixed Income Can Play an Integral Role in Any Retirement Strategy – Russell Wild

About Russell Wild, MBA, Principal of Global Portfolios

Russell Wild, MBA, is the author of Bond Investing for Dummies, now in its third edition, and numerous other books on finance. Wild is the principal of Global Portfolios, a fee-only investment advisory firm based in Philadelphia, Pennsylvania. Russell has also written for dozens of publications, often covering the finer points of bond investing.

Navigating the Critical Ages of Retirement Income Planning

Heather Schreiber, RICP®, Founder and President, HLS Retirement Consulting, LLC

Editor's note: This article is an adaptation of the live webinar delivered by Heather L. Schreiber, RICP®, in 2023. Her comments have been edited for clarity and length.

You can read the summary article here as part of the April 2023 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 Navigating the Critical Ages of Retirement Income Planning for 1.0 hour continuing education (CE) credit.

By Heather L. Schreiber, RICP®, HLS Retirement Consulting, LLC

There are so many twists and turns along the road to navigating as clients approach retirement, enter, and funnel through it. How can the average consumer possibly navigate all these rules at different ages? In addition, SECURE 2.0 has finally been signed into law, so in this article, we'll cover how to leverage some new opportunities as well.

The SECURE Act and SECURE 2.0

But what was the big thing with the original SECURE? It eliminated the stretch for most non-spousal beneficiaries. That was three years ago, but most advisors still need clarification.

The SECURE Act also changed the required minimum distribution age from age 70½ to age 72. It also permitted traditional IRA contributions beyond age 70½; it was not permissible before. If you have earned income, you can still contribute to a Roth IRA after age 70½. They merged the traditional IRA landscape to be the same, and it started to allow part-time, long-term workers to enter into 401(k)s; instead of requiring 1,000 hours of service, it went down to 500.

What is "Son of SECURE, or SECURE 2.0"? It is "Division T" of the much larger $1.7 trillion Consolidated Appropriations Act of 2023. It was signed into law on December 29th and contained 92 provisions that are retirement-related. They were mainly intended to encourage savings and broader participation in retirement plans. There are also some revenue provisions. It is broken into sections: expanded coverage and retirement savings, plans, preservation of income, and revenue provisions. There is a lot of Rothification going on in this new bill, and there is also one section designed to clarify the rules.

There are amendments and technical corrections, but there is a resounding theme of continuing to put the worker or employee in the driver's seat, enticing them to start participating in plans, mainly if they work for a small business.

Mission Critical Age 50 Retirement Planning

What do we know about age 50 and retirement planning? It is the first age at which someone can make a catch-up contribution, which had stayed the same since 2001 when catch-up contributions were enacted.

For IRAs, it has always been $1,000 since they were enacted. It has never been indexed, so part of the changes under 2.0 is that it will finally be indexed starting next year. Starting next year for 401(k)s, 403(b)s, and 457(b) plans, catch-up contributions for employees, the bill says, that had income in the prior year of the plan in excess of $145,000, which will be indexed, must be made on a Roth basis.

With Secure 2.0, catch-ups for employees with compensation in excess of $145,000 will be made on an after-tax Roth basis does not apply to SIMPLE IRAs.

Age 55 Separation from Service Rule

The age 55 separation from service is an exception to the 10% penalty. The 10% penalty usually goes away at age 59½. But in certain instances, if someone participates in a qualified plan, like 401(k), 403(b), TSP, defined contribution plans, not IRA-based plans, and they separate from service in the year they attain age 55… what does that mean? That means if I am 54 this year and get let go or I leave my job, whatever the case may be, as long as I am going to be 55 this year, the year that I separate from service, I can take money directly out of my 401(k) plan of my employer without paying the 10% penalty.

Let's return to age 50 for a second because you can substitute age 50 for certain public safety employees such as police officers, firefighters, and border patrol officers. The same thing applies to them. If they take funds directly out of the plan at age 50, they will pay tax but not the penalty. Something that changed with SECURE 2.0 is they added private sector firefighters, state and local police, and those with 25 or more years with that same employer, even if they are not age 50.

What are the finer points about the age 55 exception? One is, and I say it twice, it must come directly to the employee. All bets are off if someone takes that money from the plan and rolls it into an IRA. They have lost the ability to take money out without paying the penalty, okay? Think about the people you work with who say, "Oh, I left my job, but I need to bridge income. I need income from this pot of money." Then, it is very important then to leverage this opportunity. "You take the amount that you need directly from that plan. Take what you need and pay the taxes on it, and then roll the rest to an IRA for later money," for post-59½ money.

What happens if someone requests an eligible rollover distribution from a workplace-defined contribution plan? There is a mandatory federal withholding of 20%, which is not necessarily bad because they will set it aside for use from ages 55 to 59.

Now, if someone says, "Well, I just separated from service, and I am 53. Can I just let it sit until I am 55 and then take the distribution?" I hope you say, "No, you cannot do that." It is a simultaneous requirement in the same year.

Age 59 ½ In-service Withdrawals

A common question is, "When can my client take an in-service withdrawal from their 401(k)?"

What is a normal distribution? A normal distribution, in IRS speak, is when you do not pay a 10% penalty; the code on the 1099-R is a seven. That is what you want it to say in Box 7, which is a normal distribution. It is not a "one" or a premature distribution. But it has to occur not in the year that you turn 59 ½, like the 55 exception. It must occur at or beyond age 59 plus six months to qualify as a penalty-free exception unless you meet one of many exceptions, such as death, disability, and first-time home purchase up to $10,000.

SECURE 2.0 has added a $1,000 emergency withdrawal annually starting in 2024 across plans or IRAs. Another allowable distribution was added for those who are "terminally ill," that would be certified by a physician that the person is expected to pass within seven years. This option is available immediately. Another one is for domestic abuse, which would be the lesser of $10,000 or 50% of the vested account balance. All these go across types of qualified plans and IRAs and are effective in 2024, and they can be paid back within three years.

There is a hardship withdrawal and a non-hardship in-service withdrawal, which most people ask about. "My client would like to gain access to this because they do not like the investments in this 401(k). They would like to roll it into the IRA where they have more choices." Let me save you and your client a headache by telling you how the IRS looks at this. The portion the employee contributes on their behalf can never be taken out as an in-service, non-hardship withdrawal before age 59 ½. So, suppose the majority of their balance is their elective deferrals and a nominal portion that is the match or the nonelective employer contributions, and they are only 50. In that case, the IRS does not allow it.

Most employers usually do not have an in-service withdrawal provision that starts before age 59½, and they do not have to offer it. It's not the same as an in-service hardship withdrawal, which serves an immediate financial need that some other source cannot rectify.

Age 60 Social Security Widow/Widower Benefits

In limited cases, you might encounter someone entitled to a widow's benefit earlier than 60. Most of the time, it is 60, but 50 if they are disabled. Generally, this is the earliest age. If I take a widow's benefit that early, it will be reduced; I will not get the whole survivor PIA.

The survivor PIA is 100% of what the deceased spouse was either collecting at the time of their death or entitled to collect at the time of their death. That is the amount I would receive if I took it at my survivor's full retirement age, which can sometimes differ from the full retirement age. People are surprised that it can be reduced by as much as 28.5% if someone takes that benefit at age 60. Sometimes it makes sense, especially if they can switch to their maximized retirement benefit at age 70. That is absolutely an option.

The other thing that catches a young widow or a widower off guard is, "Well, I went to Social Security, and they told me that I cannot collect the benefit, and there is no explanation given." They do not understand why, and my first question is, "Hey, how old are they?" If they are age 61, my very first question is, "How much are they working?" and "How much do they earn?" because even though it is a widow or a widower and you would think that they have some special graces to that, a widow/widower's benefit is still subject to the earnings limitation that applies to early claims for benefits.

The same rule applies to retirement benefit claims made early, and spousal benefit claims made early also apply to survivor benefits. So, for example, this year, the earnings limitation for someone under full retirement age for the whole year is $21,240. So, if a widow or widower makes $100,000, Social Security will send them away because they are about $80,000 over the limit. They could reduce their benefits by half of that, or $40,000, more than they could ever receive in a year. They do not explain it to them.

Knowing income limits apply and at what age someone could collect a widow or widower's benefit is beneficial to help clients navigate survivor benefits, as they often go unclaimed and unnoticed, particularly if they do not have somebody in their corner that understands and knows that there is an opportunity to leverage benefits. For example, say you are dealing with a young widow or widower who has also earned income. Comparing the widow's benefit and their own retirement benefit at age 70 is important because they can take one benefit before the other or hold out before switching to the other benefit.

Suppose that someone took their retirement benefits at 62. Their spouse unexpectedly passes away, and that benefit is greater. Let us say that their spouse is collecting $3,500 a month, and they are only collecting $2,000 a month. If they go to Social Security, Social Security will say, "Well, the survivor benefit is higher. Just go ahead and take that at age 62. We will just step you up to the difference," right?

They are going to lose the lower of the two benefits. "But we will step you up to that higher benefit." No, you will not get $3,500 because it will be reduced. After all, you are below your full retirement age. But you are going to get more. That is what they will say. What they do not say is "…or you could stay on your retirement benefit of $2,000 a month, and when you get to full retirement age, then make the election to switch because then you will collect that $3,500, or 100% of that survivor benefit, for the rest of your life."

It also works the opposite, right? Say I am working with a person whose spouse dies young, and their survivor benefit is smaller than their benefit if alive and working at 70. They could elect to take just the widow's benefit as early as possible and then switch over to their own maximized retirement benefit at age 70. These are the things that Social Security will not tell you, so they are important to know.

The other important thing concerning widow and widower's benefits is that remarriage at 60 or later does not negate the ability for a survivor to go back and collect a survivor benefit from a former spouse, even a former ex-spouse. Say I was married to someone who passed away while in my 50s; for example, if I remarry before 60, I cannot go back and collect a survivor benefit from that person's record. But if I wait until age 60 or later, I can. The same would be true if I were married to that person for ten years. As long as I do not remarry until age 60, I can go back as an ex-spouse and request the survivor benefit from that person's record. Now, if I have ten years of marriage and that person is alive, and I remarry, I cannot collect anything. But as a widow from an ex-spouse, I absolutely can. So, these are critical things to remember about age 60.

Now we pivot from survivor benefits and address supercharged catch-ups. What is this? Starting in 2024 for 401(k), 403(b), 457, and TSP plans, catch-ups are increased for ages 60 to 63, a finite period. So, when someone reaches ages 60 through 63, they get to contribute the greater of $10,000 or 150% of the normal catch-up limit at that time. This cannot be used in conjunction with the special 457(b) catch-up. It is a significant opportunity to boost catch-up contributions in those final few years when people usually have their highest earnings.

SIMPLE IRAs and SIMPLE 401(k)s. Again, same thing, but a smaller amount of $5,000 or 150% of the normal limit. Secure 2.0 says that if you earn more than $145,000 in the prior year from the employer, you must use a Roth account for the catch-up contributions. This is not just for the 60 to 63 ones; they are for catch-up contributions in general. Again, this particular component does not apply to IRAs or SIMPLE IRAs because it obviously is a revenue-generating provision for the IRS. It is not a bad thing, as it is important to diversify your assets and have Roth elections anyway. These supercharged catch-ups will be indexed at the beginning of 2026.

Age 62: Earliest Claiming Age for Social Security

Age 62 for claiming Social Security is not necessarily the right age, but I will not say it is wrong. It depends on the person, but it is a permanent reduction. Generally, it forces a caveat to everything.

But when someone files early at age 62, they will experience a permanent 30% reduction to their retirement benefit unless they did a do-over and withdrew their application. Please be mindful of this when working with people who say, "Hey, I want to file for benefits now. I want also to work,"; you need to ask about this.

Anytime someone says, "I am going to file for benefits early," the very first question should be, "Are you working?" If they say "yes," "How much?" because of the earnings limit of $21,240 (2023) for someone who is under full retirement age for the whole year. People miss it, and it is not good when they miss or do not disclose it. Last year, for some reason, I got a host of questions from people that said they got LDOs, which are legally defined overpayment notices from SSA. They are not fun to receive. It could be two years when it finally catches up. They get a letter that says, "Our records indicate that you earned X amount over the earnings limit. We paid you X amount too much. Please send us a check back. Thank you very much." So, make sure that they understand if they will exceed these limits.

The earnings limit goes up to $56,520 (2023) for the year that someone attains their full retirement age and only up to the month before FRA. The good news is that the earnings limit goes away at full retirement age. Other good news is that it is truly only a limit on earned income, and it is only the earned income of the person claiming early, not that of their spouse. It is not a limit on IRA distributions or pension income.

If they have earned over this limit, Social Security withholds benefits. If they know upfront, and they should because when you file an application it asks if you are over the income limit, Social Security says, "Okay. Well, you are going to make $10,000 over the limit. So, we will withhold the first $5,000 of your benefits before paying you a cent this year." For someone who is trying to use it to supplement their earnings, this does not work well since they can only get benefits for the however-many months once Social Security recovers their excess income. Then you have to ask if there is a better way to supplement income, such as accessing home equity through a reverse mortgage as an income bridge or whatever else they have at their disposal.

What is deemed filing? If I want to collect a spousal benefit, whether I am a non-working spouse who never earned a dime or I think it will be higher than my own, my spouse has to file. But I will only collect that spousal benefit if it produces a more significant benefit than mine. If I have earned a retirement benefit, my benefit will be paid first. For folks that have a primary insurance amount of $1800 – $2,000 a month, there is no point in trying to figure out if a spousal benefit is higher because the maximum spousal benefit is roughly between $1,700 – $1,800 right now at the best-case scenario for someone who has been a higher-earning, maximum earner their entire lives.

The earnings limit applies to early or pre-full retirement age benefits as well. The maximum spousal benefit is 50% of the other spouse's primary insurance amount. What does that mean? If the primary insurance amount of the higher wage earner, for example, is $2,000 at full retirement age – that is what PIA is – then the maximum spousal benefit is $1,000. If that higher-earning spouse claims at 62, my spousal benefit is still $1,000. That is my starting point.

Conversely, if my spouse waits until age 70 to file, my maximum spousal benefit is still 50% of his full retirement age benefit, okay? Whether or not I get that full 50% depends upon when I file for it. A reduction always follows the claimer, so ensure your clients know about their full retirement age.

The reduction factors are different for spousal benefits versus retirement benefits. The maximum reduction for someone who files at 62 is 30% for retirement benefits, while the maximum reduction for spousal benefits is as much as 35%. So, be mindful that these reduction factors are different.

Another opportunity at age 62 is that a reverse mortgage becomes available. Two-thirds of people's wealth is in their home equity. That is astounding, and this needs to be considered. People think, "Oh my gosh. I am retirement savings poor," but adding all that back in can be another solution to an income problem.

What is the eligibility for this? First, the home must be the primary residence, and it must be owned outright or have significant home equity and no federal tax delinquency. The person must enroll in a HUD-approved reverse mortgage counseling program. The homeowner must be able to cover the property taxes, homeowner's insurance, and other fees. They borrow against the home equity through a line of credit, or they can receive a stream of tax-free income.

"Free income" is like music to my ears, as there are few sources of income in retirement that do not affect Social Security taxation or potentially affect Medicare premiums, such as reverse mortgage income or qualified Roth distributions. Distributions from cash value life insurance in most cases, qualified health savings account distributions, and qualified charitable distributions are other sources.

The other thing is that repayment of the reverse mortgage balance plus interest is not due until the borrower moves, sells, or dies. It is a non-recourse loan and allows seniors to stay in their homes and near their families. There is no adverse effect on Social Security benefits or Medicare premiums because the income is tax-free. It is not how much you save but how much you keep, right?

Age 63 Retirement Planning

Age 63 is not a typical age we talk about, and the reason I do is because it catches people off-guard.

Now, people working longer may still have credible health insurance coverage under an employer-based plan with 20 or more employees. But if they enroll in Medicare at age 65, then to determine what Medicare Part B premium and Part D premium they will pay, Social Security looks at their income from two years prior. They might need to pay an income-related monthly adjustment amount (IRMAA) on top of their standard Medicare premium.

So at age 63, ask clients when they plan to enroll in Medicare to avoid Roth conversions or a significant capital gain. However, situations like "I was working at age 63, and I was in the most top-earning years of my career, and now you are going to ding me for it now that I am retired" are life-changing events that they can get out of. But things like Roth conversions are not technically in the landscape of life-changing events.

Someone highly concentrated in pre-tax assets might say, "Well, I will take the hit." The good news is that when someone gets bumped into a higher Medicare premium band, it is only for one year because Social Security looks at the next year's income every year. So, 2023's Medicare premiums are based on 2021's income; next year's premium will be based on 2022 income. So, sometimes paying the piper for one year might make sense to get into a better tax position. Just be mindful of it because people do not want to be surprised when you are trying to do tax planning, things like diversifying from a tax standpoint, and forget about this point.

The IRMAA is a cliff regime; for example, if you are single and making under $97,000, your premium is $164.90 (2023); if your AGI is $97,001, they are going to pay $230.80 instead of $164.90.

Age 65 Retirement Planning

There are special Medicare enrollment periods for people who have health insurance coverage from a workplace plan that allows them eight months from when they lose the coverage. Retiree health coverage and COBRA do not qualify for a special enrollment period.

But in general, you want to remind your clients that before 65, they need to consider the Medicare Initial Eligibility Period (IEP). They need to enroll because they do not want to lose out and do not want to pay a lifelong penalty. Generally, they can enroll the three months before their 65th birthday, the month of their 65th, and the three months after. It is a seven-month enrollment period. If they miss it and do not have a good reason, like they were covered under creditable coverage, they will pay lifelong penalties for every 12 months they miss.

I will not spend much time on taking Social Security Benefits at full retirement age but know the takeaway here is that everyone needs to know when that is because a) it is the moment they can get 100% of their promised benefit; 100% of their PIA, not less, not more, and b) It is also when the earnings test no longer applies.

The primary insurance amount is based on the highest 35 years of indexed earnings. So, the longer someone works to fill those 35 years, the better for their primary insurance amount calculation. It is also the latest age at which someone will get a higher spousal benefit than their own, or let us say it is a non-working spouse; waiting beyond full retirement age to take a spousal benefit does not get you anything.

You do not earn delayed retirement credits on a spousal benefit. So, take it at full retirement age, assuming the worker's spouse has filed. Delayed retirement credits do not apply to spousal benefits. Still, they apply in the survivor world, meaning if I am a higher wage earner and choose to wait to take my benefit, my surviving spouse, a lower wage earner, will benefit from that delay.

Mission Critical Age 70

This is the latest age anyone should ever file for Social Security.

Trust me and believe that I have talked to people that said, "Well, I am still working, and I am now 73. I never filed." Do not do that because you can only go back six months retroactively to claim your benefits. So, make sure that anyone you are working with always claims their benefit on or before age 70.

Also, if they were one of the lucky ones that could file restricted, they are collecting spousal benefits now and intending to switch over at 70; know this does not happen automatically, so make sure they contact Social Security to get those benefits switched over.

Retirement Planning for Age 70½

For years and years and years, this was the age at which RMDs started. Under SECURE 1.0, it changed to age 72. The same happened for qualified charitable distributions (QCD); they have stayed at 70½ for SECURE 1.0 and SECURE 2.0, which changed RMDs for people not already taking RMDs, to 73. At 70½, this is a fantastic opportunity to leverage charitable donations with RMDs, even before that. So, someone already giving to charity should switch and pivot immediately to a qualified charitable distribution.

This only applies to IRAs, not SEPs, SIMPLEs, or qualified plans. But for someone at least 70½ on the day that they make this QCD distribution, where it has to go directly to the qualifying charity, they can do a maximum of $100,000 per year per individual that owns the IRA. And guess what happens? Instead of getting maybe no charitable deduction at all, or a nominal one because I think, for a married couple, it is like $600 if you do not itemize, which hardly anyone does anymore, the charitable contribution is tax-free. It does not hit AGI; when they reach age 72 or 73, it also satisfies the RMD up to the amount of a QCD. This is huge.

The other thing is that QCDs have been around for a while and have yet to be indexed. Starting in 2024, a maximum of $100,000 will be indexed. In the past, if people wanted those funds to go to a charitable gift annuity, the answer was always "No." With SECURE 2.0, they have added a one-time option to fund a charitable gift annuity of up to $50,000. Not $50,000 additional but $50,000 of the annual $100,000 charitable distribution limit. It can only be done once. Some limitations exist to make them suitable for charitable remainder trusts.

Again, QCDs are tax-free and do not require itemization on a tax return to take advantage of it. And once someone reaches RMD age, they can satisfy their RMD with it as well. If you are tithing for your church or some way, anyway, do it this way to at least take advantage of not having it added to your AGI."

Mission Critical Ages 72 to 73.

Folks who were age 72 by the end of 2022 continue taking distributions beginning at age 72. Nothing changes for you. But the people that were not 72 by the end of last year can now delay taking their required minimum distributions until age 73.

This is good news for people who do not need the income. The bad news is that we are now fitting RMDs into a shorter period, adding more tax to the situation and possibly more left to heirs. Most heirs now have ten years for distributions, which also has implications.

Key Takeaways

We have covered many ages.

- *Pre-age 59½ clients:* See if they can leverage the age 55 or 50 exceptions if they are public service employees. Can they leave a portion of the monies in the qualified plan and leverage that to bridge the income and roll the rest into an IRA for post-59½ use instead of using a 72(t)-payment stream? This is draconian. If they are before 59½ and still working, ensure they take advantage of these catch-up contributions.

  Consider a Roth election to diversify their retirement income. If they have historically done pre-tax, maybe start having them think about "Pay the piper now." Let's start doing a bit of post-tax elections in your 401(k) now because we do not know. If taxes are going to go up in retirement, it is a risk they take if they do everything pre-tax now.

- *Age 59½ to 70 clients:* If they are still working, assess whether in-service withdrawal opportunities exist. At age 59½, remember, if the employer allows for an in-service withdrawal provision, then that is the earliest age at which they will allow it. Again, they could stay later than that, but that is the earliest they could allow it for 401(k) for elective deferrals.

  Discuss how to maximize the primary insurance amount for Social Security benefits. Remember I said it is based on their highest 35 years of work. If there are zeroes in that calculation, Social Security does not just pat them on the back and say, "You only have 20, and we will use the 20." They use 20 of their earnings and 15 big, fat zeroes. Make sure they understand that working, even part-time, will bolster that eventual benefit by filling up those gaps.

  It also breaks them apart from being dependent on a working spouse because if they say, "Well, does it make sense for me to go back to work or work if I can just get a spousal benefit?" However, what happens if you rely on the higher earner to claim a benefit? That higher earner has to file for the benefit. You have got a double-edged sword. We want the higher earner to wait a bit longer because that will be a good bit of income during a lifetime that can also pass onto the survivor. You want to start talking about Social Security claiming strategies long before they actually do make a claim and build that into holistic planning.

- *Age 63:* If they are getting ready to retire, should they use Roth conversions to diversify their tax buckets? If they plan on enrolling in Medicare, what is going on in the year they turn 63, or the two years before their retirement date if it is later? Talk about income solutions to maximize Social Security. Is there a better way to hold off on Social Security? Use a reverse mortgage strategy to hold off on taking Social Security.

- *Are you working with widowed clients?* Leverage their worker and survivor benefits. Social Security will not offer that up as a solution.

- *Age 70-plus clients:* Has the client filed for Social Security? If they have not, they need to. If they claim, they will only pay back two years' worth of benefits, and only six months of retroactive benefits can be paid. Again, when someone hits 70, and they are getting to 70½, ask, "Are you donating to charity? Are you donating cash? Are you giving money to your church? Let us pivot and use your IRA money to do it because, pretty soon, at age 73, you will be subject to RMDs anyway." But even if you are not, taking advantage of that charitable contribution is better because if you are not itemizing, you are not getting much of a tax benefit out of it right now. You might as well switch it, do it from your IRA, and then not have to pay the taxes on it.

You always want to calculate the effects of RMDs. Start doing that in a client's late 50s, thinking about the long-term effects of the RMDs will affect future Medicare premiums, which might bump them into a different tier.

And finally, always review beneficiary designations. I have heard more horror stories about people that do not have beneficiary designations on their IRAs, qualified plans, and annuities. Whatever the case, make sure that their end-of-life wishes, and beneficiary designations are in order, and get the next generation involved. Who are the key players in their family? You want to get those people involved.

Navigating the Critical Ages of Retirement Income Planning – Heather Schreiber

About Heather L. Schreiber, RICP®, Founder and President, HLS Retirement Consulting, LLC, Retirement Income Strategist, Speaker, Writer, and Trainer to Financial Professionals

Heather Schreiber, RICP®, is Founder and President of **HLS Retirement Consulting, LLC**, Heather partners with financial, legal, and tax professionals to build holistic client solutions for retirement.

Heather prides herself in her ability to customize potential solutions to meet the needs of each client or prospect as well as her ability to turn complex strategies into easy to understand terms. In her 20th year in the industry, Heather has worked within the finest organizations including Franklin Templeton Group of Funds, AXA Advisors, SunTrust Bank and one of the largest FMOs in the country. She is frequently asked to speak at industry events, radio programs, recruiting webinars and created and led a series of bi-annual 2 ½ day intensive training events for elite advisors on effectively weaving Social Security planning into their sales process.

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Adapting Your Communication Style for More Effective Client Relations

Joseph Tabers, CSP, President of Productive Training, Inc.

Editor's note: This article is an adaptation of the live webinar delivered by Joseph Tabers in 2023. His comments have been edited for clarity and length.

You can read the summary article here as part of the April 2023 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 Adapting Your Communication Style for More Effective Client Relations for 1.0 hour continuing education (CE) credit.

By Joseph Tabers, CSP, President of Productive Training, Inc.

To understand our client's communication style, usually, the first place to start is with ourselves. Think about what comes easy for you; what are you good at? For example, some people are good listeners, some are good at asking questions, and some are good at patience.

Today's communication styles are well documented. We need to appreciate the differences knowing that we will not change the communication style of another individual, client, or otherwise. The best bet is to start with our communication and then adapt to theirs to look for better, tighter connections. We should be able to appreciate their strengths, respect their weaknesses, and work within them.

Think about where you want to adapt to your communication style and where to improve. The goal of adapting our communication style to that of our clients is to build more trust, rapport, and better connections so that you have lasting and sustainable relationships.

Why Bother Adapting Your Communication Style?

I once had a client who spent over $1 million asking clients and customers, "What do you want when someone is servicing you?" This is still a valid question.

First, people want us to be understanding and understand their situation. Everybody thinks their situation is unique. In many ways, they are, but they want us to understand what they are dealing with, their concerns and fears about the future, and their current finances.

Second, they come to you because you have knowledge. It is about more than what you and I know but how we can use what we know to help them.

Third, take responsibility. People like us to provide answers and take responsibility for getting them the things they need to make an informed decision.

Finally, we need to show we care, have a heart for right, and care about them and their future.

Brief History of Communication Style Assessments

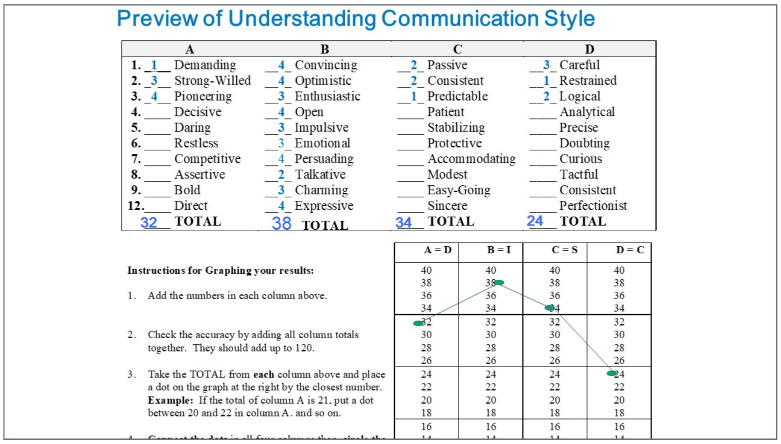
There are over 100 different style assessments, be it personality style, behavior style, or communication style assessments. The good news is that they all go back to core research. In 1921, Carl Jung defined four main functions that all human beings have: sensing, intuition, thinking, and feeling. He then looked at the range of how it is different for people.

In 1928, William Marston wrote a book called *Emotions of Normal People*. Before that, there were many studies on deviant and poor behaviors, and no one studied normal behavior, and William Marston defined ranges for normal behavior in a good, healthy way. Beyond that, Keirsey-Bates, Myers-Briggs, and other assessments started in the mid-60s and early 70s. Style assessments all have similar core traits in that they try to define a range of behavior that we all express when interacting with one or more people.

Then finally, the military started mainstreaming style assessments in the 1970s. Corporate America then jumped on board, and they have been utilizing them ever since. Over 15 million assessments have been taken over the years. Over the last 20 years, our firm has done thousands for our clients. Ninety-nine percent of the time, people say they are very valuable and helpful. Once in a while, someone says, "Yes, I pretty much knew that about myself already." That is a pretty self-aware person, but even then, they will argue that it is nice to have it in black and white and in print.

A Preview of Understanding Your Communication Style

Most assessments have you compare things, such as words or adjectives that describe your behavior.



Preview of Understanding Communication Style

	A		B		C		D
1.	1 Demanding	4	Convincing	2	Passive	3	Careful
2.	3 Strong-Willed	4	Optimistic	2	Consistent	1	Restrained
3.	4 Pioneering	3	Enthusiastic	1	Predictable	2	Logical
4.	___ Decisive	4	Open	___	Patient	___	Analytical
5.	___ Daring	3	Impulsive	___	Stabilizing	___	Precise
6.	___ Restless	3	Emotional	___	Protective	___	Doubting
7.	___ Competitive	4	Persuading	___	Accommodating	___	Curious
8.	___ Assertive	2	Talkative	___	Modest	___	Tactful
9.	___ Bold	3	Charming	___	Easy-Going	___	Consistent
12.	___ Direct	4	Expressive	___	Sincere	___	Perfectionist
	32 TOTAL	38	TOTAL	34	TOTAL	24	TOTAL

Instructions for Graphing your results:

1. Add the numbers in each column above.
2. Check the accuracy by adding all column totals together. They should add up to 120.
3. Take the TOTAL from **each** column above and place a dot on the graph at the right by the closest number. **Example:** If the total of column A is 21, put a dot between 20 and 22 in column A. and so on.

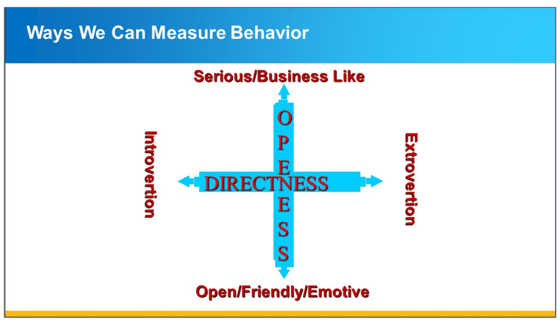
A = D	B = I	C = S	D = C
40	40	40	40
38	38	38	38
36	36	36	36
34	34	34	34
32	32	32	32
30	30	30	30
28	28	28	28
26	26	26	26
24	24	24	24
22	22	22	22
20	20	20	20
18	18	18	18
16	16	16	16

For example, in this assessment, if you had to think about the four qualities on the first row of each column, *Demanding, Convincing, Passive, and Careful*, which is more of your natural style? Are you more demanding, or are you more convincing? Are you more passive, or are you more calculated and careful? You choose the one most like you in each category and give it four points by putting a four by it. You would put a one by the one that is least like you. There are four choices per category. Scores are added up, and a communication style is assessed.

Ways We Can Measure Behavior

We can measure behavior through assessments and observation. A common assessment today is based on what we call the DISC model, or D, I, S, and C.

The first thing that is measured is that left to right scale. Some call it the "introvert/extrovert scale" or someone who is more outbound in their communication versus someone who is more reflective and inbound in their communication.



Think about that for a minute. If you had to put a tick mark on the line here somewhere, where would you be? Would you be a little further to the right side? Are you more extroverted in your approach? In other words, are you a conversation initiator? Are you first to stick out your hand and say, "Hi, I am Joe, and you are…?" The more often you do that, the more you start conversations or initiate, the more likely you are comfortable, and you have more of those traits to the right. Likewise, if you are a good listener and more reflective and introspective, you probably have more of those traits to the left.

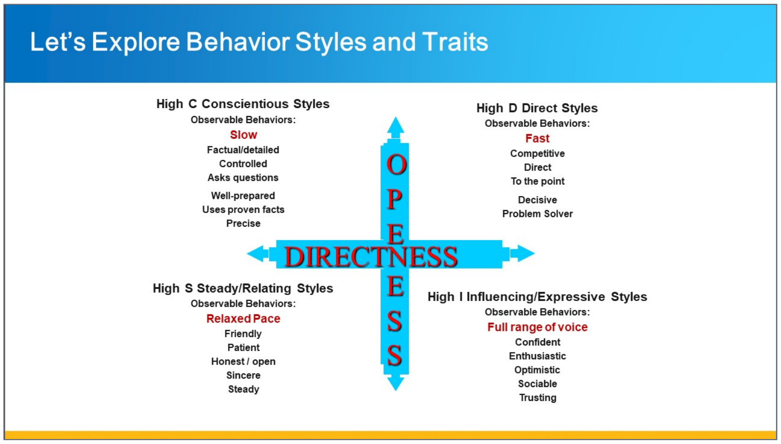
Some people also use an energy question. Do you get more energy when around people? Does that build you up and excite you, or do people drain you? Would you prefer instead to work alone? "Leave me alone, and I can get my work done." Sometimes those come into play with behavior as well.

The second thing that gets measured is the top to bottom and what we call openness or sometimes known as responsiveness, or that vertical line. How responsive are people with their face and their expressions? The more serious and poker-faced someone is, the more likely they are to be above the midline.

The more open and emotive they are, the more likely they will show their poker hand. They are showing their reaction. You can see this dynamic in your family and friends. Introversion, extraversion, seriousness versus openness, and friendliness or more emotiveness. How about you and some of your favorite clients, or how about you and some of your more challenging clients? Think about the dynamics that go on there.

I mentioned the acronyms D, I, S, and C earlier—these four traits we all have in our personality to different degrees. Often what happens, though, is one or two of those will rise higher in your natural style than the others, just like they will in your clients.

The "D" quality is when someone is more serious and they are more outspoken, sometimes known as direct and even decisive. The joke about that is the "git 'er done" style or "Okay. Let's do this. Let us get down to business. I do not have time for small talk." So, the direct style, the more of that someone has in their personality, the more obvious it is to you.



The next style still on the extraversion style you will hear about is the "I" quality. The I quality is for what we call influencing, and some call it the expressive style. Are you someone who, again, is still extroverted but not as direct, candid, or unfiltered, or are you more of a people person where you do show emotion and you try to influence them with your words, your stories, etc.? Both of those qualities, the D and the I qualities, are more extroverted.

The "S" quality is for steady, stable, sometimes called easygoing or amiable, more laid back, and more likely to think about things. They still like relationships, are friendly, and show emotions but are not as much of an initiator. They will reciprocate a conversation if you start it, but they may not be the first to initially stick out their hand and show some assertiveness.

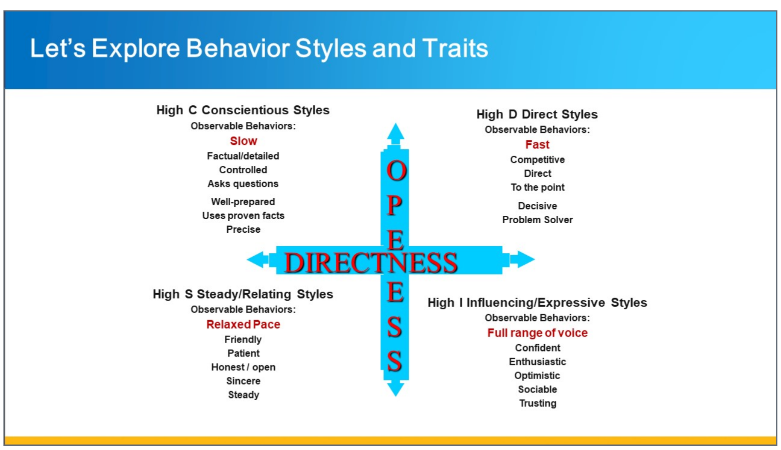
The "C" quality is conscientiousness, sometimes known as an analytical quality that basically is the stereotype of the thinker. It is someone who gives things thought; they like facts, information, and data. They may ask more questions than the average person.

Both of these are very task-driven behaviors on the top. The D and the C are task focused, whereas the bottom styles are more relationship focused. Dynamics that go on with your clients might be whether they want to get right down to business versus do they want to get a cup of coffee or tea, settle in, and talk a little bit about you and them. It is going to be different for different people.

For example, you can easily notice a person with a high D quality. They would say, "Oh yes. I am pretty direct, and I am pretty blunt." The higher the D, the more direct, maybe even pushy or blunt, they might come across, but you also notice this person has the C quality. The higher the C, the more task oriented. They have a double dose of task behavior. I and S are more relationship in the center. The higher the S, usually the slower the pace. The lower the S, in this case, demonstrates that this is a fast-paced, "get on with it" kind of person.

How Do Behavior Styles Apply to Client Interactions?

To that point, then, let us look at how this all relates.



If someone observed you, what would they see? Let us start with the "D" quality. If 70% or more of your style is D, people will notice you are direct in your communication. You are competitive. You are to the point, problem-solving, driven, and so on. It is easy to spot the D quality because it is usually someone very comfortable and confident with themselves; some would even say, at times, unfiltered.

The "I" quality is still confident but more people focused. Enthusiastic, sociable, and trusting, they like building those relationships. You'll see a full range of voice used with people in the upper half, with the D quality being more serious in their voice. So again, some similarities between the two on the right, but definitely differences in task focus versus relationship focus initially.

The "S" qualities are patience, friendliness, candidness, honesty, sincerity, and maybe a little bit more moderate in their approach, even calculated at times. The "C" quality is a slower pace, more factual, comfortable with silence, and more controlled in their demeanor.

Of all those traits, first, which ones are yours? Once you know your trait, then ask yourself, which clients do I already hit it off with easily? Very often, likes to attract likes. Someone might like your style because they have a similar style, or it is possible for someone to like your style because you have something they do not have. You may be more analytical than they are, and they admire that. It is good to start thinking about what has worked for you in the past, who are those relationships you connect with now, and where are the ones where it is a little more oil and water.

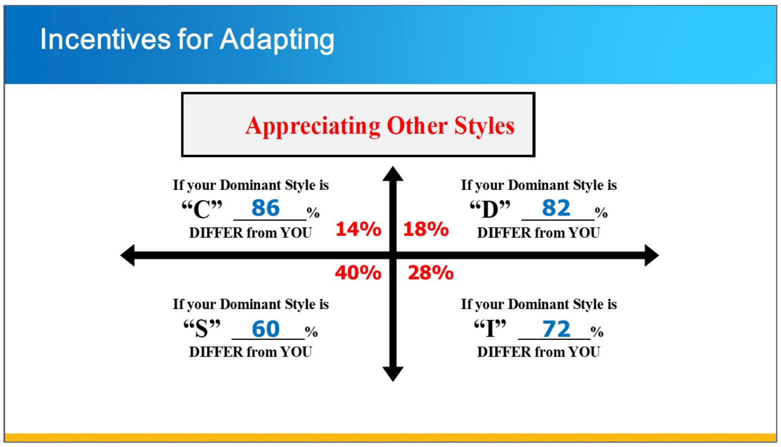
Ask yourself, "What strength do I currently have when dealing with clients?" You could say you are a numbers person. Anybody in the financial field may have that gift of numbers, but some of you had to work harder. Some people are wired that way and think that way; others choose it, and they have to work at it and learn it.

When working with other people, what is a friction or tension point extreme where it would be like mixing oil and water? It might be directly opposite or diagonal to your style.

National Averages for Communication Styles

Let's look at some natural averages because many people want to know who is the most common of those styles. What should I expect a higher percentage of? I cannot say this for you because, obviously, national averages only represent some people, and people coming to you may be more financially astute than others. They may represent the general population.

If you had to take a guess, which style do you think has the most people? Yes, you would be correct for those who said the S style. Forty percent or most people that fill out assessments have more of that steady, stable S style.



It makes sense if you think about it because they are the worker bees, often those who stay on until retirement. They are the ones that will work hard at their savings. They are stable, steady, and reliable. A lot of those are the average workforce.

The I quality represents the second most common style. It could be a school teacher or salesperson, but people that like people and are in a profession where they enjoy using their social skills. Twenty-eight percent have more of that emotive quality which may be for you might be a good reminder that, yes, we all know that money affects emotions, but maybe even more so for a high percentage of the population here.

Only 18% have the D quality, which for many, is their greatest challenge. But the C quality makes up 14% of the population. Not everybody is an accountant, and not everybody is a financial planner or an analyst. Even though you may have friends and a lot of them in that upper left corner, if that is you, it is still not the highest national average. Be aware of that. People are wired differently. They all do not have their highest bar graph where you might have your highest bar graph. Another way of saying all this is that there is a good incentive, as the title of this slide says, for adapting.

To say it another way, we will flip it inside out here. Even if you have the S quality, 60% of people do not have that S quality even if you might have it. Or to say it with the I quality, 72% may not be as social or friendly as some of you are if you have a lot of that high quality. Eighty-two percent, or eight out of 10 people, do not have that D or direct "get her done" approach. With the C quality, 86% aren't as factual and well-prepared.

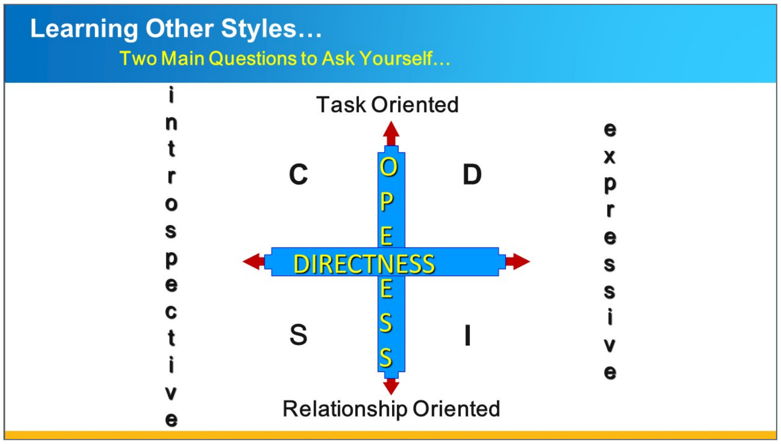
How to Adapt Your Communication Style for Your Client

Clients might come to you because they will say, "I am not good at math," or, "I could do this, but it just makes me stressed." There is something about facts and details that some people love, and maybe that is you, and some things that others do not like, like planning and crunching up numbers. So, it is a good reminder and incentive for us to make an effort to adapt.

I have heard people say, "I just treat everybody the same." Well, and good to a point, but that is the Golden Rule. Some of you may have heard that the Platinum Rule is to treat them the way they want to be treated or adapt to their style in a way that works for them.

Let us say it is two months from now, and you are saying, "Joe, this is all well and good, but how am I going to remember or even begin to figure out where someone in my client base is at?" Well, we all can ask questions.

A couple of questions you could ask yourself are the left to right. What am I seeing? What am I hearing if it is a phone call, initially? Am I hearing someone more introspective, reflective, and slower paced? Am I hearing someone more expressive? So, decide if they are to the left to right and put a flag in your mind. What are you seeing and hearing more?



If you meet someone face-to-face, what do you see in their body language? What do you see more in their approach? Are they more expressive, or are they more reserved and introspective? Once you ask that question and answer it yourself, you can go to the next one, top to bottom. Am I seeing some of that "let us get down to business" task-oriented? Are they asking very factual questions? The more task-oriented they are, looking at their watch, "get her done," the more likely they have the C or the D quality, more of the task behaviors.

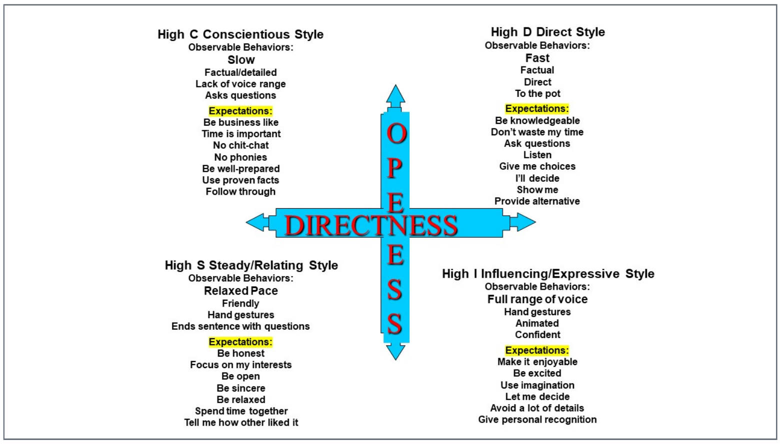
Then, you will also know from their communication whether they are on the left side or right side of that. If they say, "Let me tell you about my grandma and why I am here. "She did not plan," or "She did plan well," where you get stories that will give you hints about their relationships and that they need to share that with you. You do not have to be a psychologist to remember this. It is two questions. What do you see more? What do you hear more? More tasks versus relationships? More introspective versus expressive, outbound?

Also, think about other basic adaptations of your style. What would that look like if you stepped into their world or comfort zone?

Let's say a client is direct. "Look, I only have 30 minutes. Can we get to this and get this done right away?" If you have that, what can you do? Project more of a sense of urgency. Speed up a bit. Get to the point faster. If you ask questions, keep them short. "Do you want me to get back to you by phone or email?" Go into their world. If you want to drive them crazy, slow it down and ask 100 questions. They will answer questions, but they like fast-paced and to the point.

Let's say you need to adapt more to the I quality, or maybe this is you. If you are more of a people person, ramp it up, be more task-driven, and be more objective.

These are basic, initial adaptations that you could take. Speed it up. Slow it down. Be more task-focused, more relationship-focused. You probably do it already with your relatives and friends intuitively; now, do it more intentionally to adapt your communication for more effective client relations.



If you know what a client expects, you can prepare for that meeting, assuming you have done a little observational awareness beforehand. For example, not surprisingly, the D wants you to be knowledgeable, not waste their time, ask questions, and get to the point. Give them options and choices that let them have control and make the decision. On the other side of the task, the C style does not want much chit-chat, and they do not want someone to be winging it. They want well-prepared, use facts, and show where you came to your conclusions. So again, very factual-oriented, and you can meet their needs that way.

For the lower half, as we already talked about, make it an enjoyable experience, maybe even use your imagination. Talk about what planning will do for them in the future five or ten years. Again, appeal to their need to make this a fun experience, unlike a trip to the dentist's office. Then lastly, the S style. They are looking for a genuine person they can trust in a relaxed fashion, not feel rushed out the door by someone who sets aside a block of time. Like good bedside manners with the doctor, right? You have time to ask the questions you want and feel they have your best needs in mind.

Ways to adapt your communication style:

1. If you want to think about high-octane clients with more D quality, get to the task quickly. Do not waste time. Be business-like, be prepared, and be serious. They do not need a lot of smiles and glad handling. Think of a businessperson, a CEO with a tight schedule; "I am already late. I have to run."

2. The I quality, the lower half of that extroverted side. They do like time for socializing. So, if you were to ask questions about family and friends, or if you were to ask questions about how their parents planned or did not plan for retirement or the future, and you say, "I want to make this an enjoyable experience for you," and begin talking about the exciting side of it and what that means for future trips and vacations; there are lots of possibilities there. Some of you already have some of this naturally in your DNA. Some of you may have to work at smiling more. I say that jokingly, but I know sincerely that when I work with some people that are serious types, sometimes they do need to work at lightening up and making it a more enjoyable experience.

3. For the S quality, think of the average worker that wants some time, and they do not want to be rushed out the door. Sincerity is the mantra here. Show that you care, be fair, respect their time, and if you need to, reschedule a follow-up or second meeting so they get their questions answered.

4. Finally, the C-quality clients will likely come prepared. They might even have some work already done on their research and give it to you. They may have already compared you and your approach to others, so you can even ask those questions. "Have you compared us to anyone else? Tell me what you did or did not like about some of the other planners or folks you met with." Be organized, be prepared, and know what questions you want to ask them. "I have a few questions I want to ask you to ensure I get some answers." Pre-questionnaires might come in handy, too, for them to fill something out before you meet with them to make you even more prepared.

Key Takeaways

Some people also hear about things like the Myers-Briggs. Our point with that is that it takes and divides each of these four components into basically four more quadrants. You end up with 16 types in the Myers-Briggs. It's a good tool if you have the time and resources to do that, but it can also be daunting to remember 16 different traits. So, let's keep it simple here with just four quadrants for starters and the two questions in Item 3 below to ask yourself.

1. Knowing your most dominant trait is good, but *work to self-manage it.* Avoid over-extending it!

2. When dealing with other styles, reflect on their *style preferences* to better connect.

3. When working with others, ask yourself the two questions for better understanding:
   a. Are they more introspective/reflective or outspoken?
   b. Are they more task-focused or relationship-focused?

4. When in doubt – listen, observe, appreciate, then "adapt" your communication style as you go to help build more trust and reduce tension.

Adapting Your Communication Style for More Effective Client Relations – Joseph Tabers

About Joseph Tabers, CSP, President of Productive Training, Inc.

Joe is an expert in improving workplace presentations, interpersonal communication skills and relationships. Over the last 25 years his team has helped more than 450 organizations and thousands of individuals increase their workplace effectiveness by enhancing their communication skills. As a proven professional speaker, author and communication coach, Joe will help you connect better with audiences from high-level professionals to frontline workers.

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