



Retirement Income:

Solid as a Rock?

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Is Your Retirement Income Solid – Or Shaky?

In the past, a solid income plan in retirement has been financed through a combination of pensions, Social Security and personal savings. By relying on these three funding mechanisms, retirees could count on income to last for the rest of their lives.

Consider the humble three legged stool. The three legs of the stool form a solid sitting surface. For the past 30 - 40 years, this three legged stool analogy worked for most retirees. 1/3rd of income needs were funded with a company pensions, 1/3rd with social security, and the final 1/3rd through personal savings.

But what about now? Which leg would you guess is the shakiest?

Many people might answer “Social Security”, but in my opinion, pensions are in the most danger.

According to the most recent survey by Towers Watson, in 1998, 90 percent of Fortune 100 companies offered a lifetime pension to their retirees. Now that number has almost completely flipped. By 2012, only 11% of these large companies offered pensions to new hires.

Of course, the reason for the decrease is easy to figure out. Pension plans are extremely expensive. After all, to fund a guaranteed income for life, the pension plan needs to take on two big risks – stock market risk and longevity risk.

Pension plans are subject to very stringent funding requirements set forth by the Department of Labor. Every year a team of actuaries determines how much the company needs to contribute to the plan to meet their obligations to their retirees. What if the year happens to be 2008 when there’s a big market correction followed by a recession? Then the company has two problems – first of all, they must make up for the market losses in the pension plan – at the same time that their revenues may be hurting because of the recession.

The second risk is longevity. Consider this case in point:

This individual had the following health issues in his life

- Suffered 1st heart attack at the age of 34.
- At age 39, an on the job injury almost left him paralyzed.
- For the next 13 years was addicted to painkillers.
- At the age of 56, had another serious heart attack.
- Is a type 1 diabetic.
- Has had pulmonary fibrosis
- And last but not least – has prostate cancer.

With all these health issues, how long would you guess that he would live?
Age 65? Maybe 70? Could he make it to age 75?

On March 16th, 2014 Jerry Lewis turned 88 years old!

Employers have that same risk – that every medical advance means that they will need to fund their employee’s retirement for a very long time. That is why employers have turned to 401(k) plans.

Regrettably (in my opinion), employees are the losers in this change. Instead of a professionally managed portfolio and income for life, their employers now furnish them with an 800 number and a PIN.

Social security is the second leg of the income stool.



Jerry Lewis Publicity Photo
1960's – Author Unknown

In 1935 when Social Security was started, the average life expectancy for women was 63.9 years and the retirement age was 65. Therefore, it was assumed that most people would not collect Social Security and it was a fallback position for those who lived longer lives. Today, due to the miracles of modern medicine, life expectancies have dramatically increased. According to the 2009 LIMRA *Retirement Income Reference Book*, if you are over the age of 65, there's a 50% chance that you will reach age 86 and a 25% chance that you will survive to age 92. That means that if you take early retirement from Social Security, there's a 1 in 4 chance that you will be retired and drawing Social Security for 30 years!

At the same time that life expectancies have increased, the number of workers to retirees has dropped. According to Social Security, the number of workers to retirees is now only 3.3 – vs 16.5 in 1950.

Will Social Security disappear? I'm no politician, but I would guess that Social Security will be here for the foreseeable future. However, I would guess that some adjustments will need to be made. They may include:

- Increase the 7.65% tax rate for current workers
- Increase the amount in wages that are subject to tax
- Increase the tax that retirees pay on their benefits from the current maximum of 85%
- Increase normal retirement age
- Eliminate the early retirement option
- Decrease the inflation adjustment
- Some combination of all of these

The bad news is that with the decreasing ability to rely on employer funded pensions and government funded Social Security, retirees are going to have to rely more and more on their personal savings to fund their retirement needs.



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