HOW TO WEATHER THE 'PERFECT STORM' FOR RETIREES

With life expectancy and retirement age increasing, planning for retirement can be daunting. At a time when solely contributing to a 401k is no longer a sufficient safety net, four local financial experts talked with Carolyn Jones, Market President of the BBJ, about how to strategize for the next phase of life. Northwestern Mutual's Managing Partner Aaron Miller as well as Advisors Michael Raposa, Tom Mitchell and Doug DiCerbo lent their expertise in retirement distribution planning.

BBJ: Thanks everyone for joining us today and shedding light on such an important topic. Let's start with you Tom - how does a person approaching retirement deal with market volatility?

TOM MITCHELL: We like to use the 3 bucket approach to protect from market volatility. The "Safe Money Bucket," "Roller Coaster Bucket" and "Home Run Bucket." The home run bucket is the best use of a dollar type of investment, potential for bigger returns, often less liquid. Examples of this Include company stock options, real estate, private equity or reinvestment back into a business.

The roller coaster bucket Includes stocks, bonds, mutual funds, ETFs. This bucket on average has positive returns four times out of every five years on average. However, it goes backwards one time every 5 years. This is called a correction. If we know it's going to happen, we need to have a plan not to sell into it when it does happen. Selling in a down market is something we work very hard to protect our clients from.

Lastly, the safe money budget consists of two to five years of cash to cover two to five years of expenses. The safe bucket is only tapped when the other buckets are not performing. The safe bucket allows the roller coaster bucket to be more aggressive by owning more equities and less safe fixed income investments therefore providing more income. In wealth accumulation, ROR is one of the most important details to gauge an investment. However, in retirement, income planning the sequence of returns is a humongous risk. The safe money bucket neutralizes this risk.

MICHAEL RAPOSA: Historically the general advice was to "get more conservative." In fact the old thinking was the 4 percent rule in retirement. Basically, one would be able to comfortably withdraw 4 percent of their investments year over year and not run out of money. This however was designed when 10 year government bonds were yielding 7.5 percent (now they are under 3 percent).

Given this is the case what we are recommending clients do is continue to take on more market exposure into retirement, but at the same time make sure they have a stock safety plan in place. We know historically the market turns negative every five to six years. We also plan that most clients will have a 30+ year retirement. So we generally recommend clients have between two to five years of safe money when they get to retirement. And if they do have this safety net in place, they can then continue take market risk into retirement and not be forced to sell equities in a down market.

Again the old thinking was that retirees would put money in CD's & Money Markets, but today these are really low yield and high tax. And so many of the buckets retirees have typically used have also fallen flat. So the newest research coming out of places like the American College and Wharton have shown well-structured cash value life insurance plans can be a great alternative.

DOUG DICERBO: One of the things we do well to help client's manage market volatility is systematic reallocating & rebalancing. We communicate to clients that when one asset class is doing well we will be selling some of it and rebalancing to other asset classes that are out of favor. This sets in motion a systematic approach (selling high/buying low) to asset allocation and helps us manage volatility in the overall markets while taking some of the emotion out of the investment process.

AARON MILLER: One of the common mistakes people make when thinking about MV in retirement is underestimating just how long retirement will last. People often times misdiagnose retirement as an event. Meaning that they turn 65, retire and everything changes the next day. The reality for many of our clients is retirement is more of a career change, and they are experiencing 25,30 even 40 year retirements and with that kind of time horizon you need to make sure they don't over rotate to being too conservative. Instead we want to think about

diversifying your assets based upon your time horizon not your age. Ultimately breaking down your wealth in different buckets to take advantage of both the good and bad of market volatility. The reality is if you are able to implement some of the strategies the others already discussed, you can often take more "risk" in your portfolio knowing you have protected your downside risk.

"31% of American workers have no savings set aside specifically for retirement.

- Social Security Administration, 2017

BBJ: What does legacy mean to your clients and how do you plan for it?

DOUG: Legacy means different things to different clients. As an example, a business owner who wishes to pass on a family enterprise may have a much different view of legacy than a physician or attorney with a very large retirement plan. To me legacy speaks to the direction of a couple's or individual's capital at death. This may include traditional stock market investments, privately held business interests, or personal assets such as a primary residence or other personal property. To avoid things like the probate process, communication issues when someone is ill, guardianship, and potential state or federal estate tax issues we encourage clients to engage a team in the estate planning process. In the end your capital will go one of several directions. These include charitable interests, income or death taxes, or your children or grandchildren and other heirs. With some thoughtful planning a client can create their own legacy and make sure that capital goes in the direction of their choosing.

AARON: My experience is that legacy can mean many different things to different people, but ultimately it is a client's desire to want to leave something behind to someone or something they care about. Said differently, it is important to most of our clients to not die penniless. This is a great ex-ample of why people should make sure they have a comprehensive financial plan that deals with the realities of retirement. When we talk about distribution planning we typically think about that while we are alive, but what assets we leave behind and how they get distributed at death can have a huge impact on the legacy we decide to leave. The best approach is to have a real deep understanding of those wishes and a plan to ensure they can happen without sacrificing your own retirement lifestyle. Our experience is that most people will leave behind something but without looking at all of your assets (real estate, business interest, life insurance, cash etc.) you could be end leaving a fraction of what you were hoping to.

TOM: We also find that people's thinking shifts during different phases of life. I have seen that once clients become grandparents, their views on legacy planning change very rapidly and become very focused on making sure that their grandkids will always remember them.

BBJ: One of the biggest risk I see people facing in retirement is the increasing cost of health and long term care. What are some things you are seeing in the marketplace to help protect against this?

DOUG: Unfortunately, my family has had firsthand experience with this issue. My mom is in the fifth year of an Alzheimer's diagnosis that showed signs of being an issue as early as eight to 10 years ago. We have had a full view of the cost of care both at home and through the various stages of the illness. The checks were modest at first (she forgot to take her medications). A nurse to remind her was $250 a month. Five years later we have 24/7 care in a nursing facility that costs $13,500 a month and continue writing monthly checks today. As it relates to the prior question (legacy) we encourage clients to think today about issues that may be a risk to their and their spouse's assets down the road. It's never too early to begin planning for these risks if

DOUG DICERBO

Originally from Upstate New York, Doug DiCerbo joined Northwestern Mutual in 1995 after graduating from Hartwick College, and has since been helping his clients secure their family's financial future for over twenty years.

Doug has been a leader in The Boston Network Office, as the Estate and Business Planning Specialist. He participates in the management and mentoring of new financial representatives, as well as teaching courses to expand the service we expect.

During his time at Northwestern Mutual, Doug has accomplished many professional milestones. He qualified for the Million Dollar Round Table (1999-2017), obtained his Chartered Life Underwriter (CLU®) designation, and qualified as a top producer with Northwestern. He holds his FINRA Series 6, 63, 65, and 7 licenses, as well as his Life, Accident, and Health insurance licenses. Doug and his wife Erin live in Lexington, Massachusetts with their three sons and two daughters.

AARON MILLER

Aaron Miller, graduated from the University of Connecticut Magna Cum Laude in 2003. He started his career with Northwestern Mutual in 2003 as a financial representative. He quickly moved into leadership, holding management positions of College Unit Director, Field Director and promoted to Managing Director in 2007 of the Northwestern Mutual Woburn District Office. Aaron was appointed Managing Partner of the Downtown Boston office in October of 2016. Aaron is a huge Boston sports fan and an active board member for Horizon's for the Homeless Children where he was the recipient of the Northwestern Mutual Community Service Award in 2015. Aaron and his wife Lauren, have two children, Bailey and Max. They enjoy spending time in their community, cooking together, and relaxing at their beach house in Maine.

THOMAS ("TOM") W. MITCHELL CFP®, CLU®, CHFC®, CASL®, RICP®

With 25 years of experience and expertise in financial planning, Tom Mitchell credits the success of his practice to dedicated financial planning and four specific areas of focus: accumulation planning, retirement planning, estate planning, and insurance planning for high income and high net worth families. A Wealth Management Advisor with Northwestern Mutual, Tom and his team rely on detailed data gathering, rigorous analysis, and the use of research and evidence-based solutions in the pursuit of planning excellence. In addition, they have, over time, accumulated multiple certifications and designations to gain a well-rounded expertise and body of knowledge relevant to retirement income planning and strategies. Tom lives in Boston with his wife Sarah and their daughter Mackenzie. He currently sits on the Board of Directors for the Boston YMCA and is a former Chairperson for the Boston Estate Planning Council.

MICHAEL RAPOSA

Michael began his career with Northwestern Mutual in 2006, after graduating with a Bachelor of Science Degree in Finance from the University of Pittsburgh. He is the Life Insurance Specialist in the Downtown Boston office and a member of the National Association of Insurance and Financial Advisors (NAIFA). Since 2016, Michael has qualified for Forum, represents the top segment of Northwestern Mutual's industry-leading financial advisors, and most recently completed his CFP in March of 2018. He and his wife live in Charlestown, MA and are expecting their first child in October 2018. He enjoys traveling overseas, attending Boston sports games, brushing up on his US history, and giving back to his community.

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clients have assets to protect.

MIKE: To Doug's point, the most critical thing clients can do is have an estate plan. A lot of clients don't have an estate plan at all or maybe they just have a basic will which will generally not address the issues of health and extended care. We try to make sure clients have an attorney with expertise in the estate planning & elder law space. When it comes to long term care or health care, often time it's the smallest documents that have the biggest impact such as health care proxy, power of attorney, HIPPA form and a living will.

AARON: Unfortunately my wife and I became experts in the last 18 months as my father in law started to show signs of dementia and we quickly learned that things like Medicare, Medicare supplement, Medicaid and the like are not designed for conditions like dementia and others that are long term in nature. Fortunately for us, my father in law had a really well designed long-term care policy, so his assets are protected but more importantly he is getting quality care and my wife can focus on providing care for our kids instead having to give care for her father.

BBJ: What can people do now to put themselves in a position to minimize taxes in retirement?

MIKE: A lot of the traditional guidance says when you retire you'll be in a lower tax bracket. What we find however is a lot of our clients have a tremendous amount of their retirement money in tax qualified plans. Unfortunately for them, these dollars are all countable as ordinary income at distribution. And those above certain income levels are also taxed on social security and most pensions. We found that one of the biggest complaints from clients is how much they still pay in taxes during retirement.

Often times this is a problem to best solve with a client years before they retire. When someone has time they can build up after tax and tax deferred investments. In doing so retirees have multiple buckets to withdraw from it gives them so levers to pull and minimize their income tax rate. We feel this is a big differentiator in terms of what we do. By having tax diversification our client can then have a bit more control over the taxes they will pay year to year. If income taxes go up and capital gains taxes are lower, it may be best to liquidate from accounts that are subject to capital gains. One idea is to contribute to a Roth 401(K) instead of a traditional 401(k) if possible, we find many clients don't know this is an option. The benefit being these distributions will be tax free in retirement and not subject to RMD's. Another relevant strategy is utilizing an efficiently designed life insurance program that is guaranteed to grow every year and the cash value can be with-drawn basis first.

DOUG: In my role as the business and estate planning specialist in Boston for the past several years I have had unique exposure to the impact of estate taxes, income taxes, and capital gains tax when planning for legacy and retirement income distribution for older clients. These are issues that can affect even a modest estate of $1 million in Massachusetts. Most individuals who own a home near Boston that is paid for have a net worth in excess of 1 million. If they own assets in addition to this or a family business and commercial real estate, the implications of taxes during retirement and at death can be significant. Individuals and business owners should consider the long term impact of taxes well before they reach retirement. Advance planning can be very powerful for mitigating or perhaps eliminating the tax burden during retirement and at death.

BBJ: With people living longer, what are some problems this can create and what thoughts do you have on how to plan for this?

AARON: In looking at all the different challenges a person faces in retirement distribution planning, this may be the most significant. Longevity is essentially the accelerant to all other risks thus making it something that needs to be looked at in every situation. Regardless of what happens in the market, we know the value of your assets will erode each year by inflation alone, so the longer you live the more erosion that takes place. Therefore, one of the key strategies we have seen is to make sure that you have created some income streams that will continue as long as you do. This helps compliment whatever assets you have accumulated along the way. Income streams not only help smooth out your plan, but they essentially act as a fence around the rest of your wealth.

TOM: The perfect storm is now brewing for future retirees: social security is underfunded and will most likely not be what is was to our parents; pensions went the way of the dodo; people are living longer and running out of money.

We need to focus on the behavioral side of retirement planning that is not all about the numbers. We are concerned with low stress and being happy financially, and less worried about money like they have been their whole lives. Having a financial plan that is stress tested annually, having multiple guaranteed income streams, working with an advisor who knows you and is there for financial guidance at every turn in life.

DOUG: Taking care of both sides "risk & accumulation planning" helps us think not only about long term accumulation but about the risks of living a very long life. Northwestern Mutual has helped build tools to take some of the emotion out of retirement income uncertainty. These tools help our clients and us predict with more certainty the likelihood of retirement success.

MIKE: The latest thinking and research is saying that having guaranteed income streams will increase your likelihood of retirement success. Success is defined by not running out of money. Among those income streams people typically will utilize are: social security, pensions and various income annuities.

The old school of thought was someone would stop working, collect a company pension and rely on social security. People expected to retire at 60-65 and probably pass away in their 70s or 80s. Now, the new school thinking and research revolves around the fact that most people don't have a pension and they are worried about relying on social security. Because of this financial intuitions have put together a lot of strategies around replacing these options. Vanguard found in a study from 2017 that a healthy 65 years couple had a 45 percent chance of at least one of them living until age 90 and an 18 percent chance of living until age 95. As a result, income annuities have become more relevant because they reward clients for living longer while taking on less risk. There was some landmark research done by Dr. Michael Finke and what he found was that adding income annuities into your retirement plan reduced the risk of outliving your assets by 24 percent and actually increased the size your legacy at death.

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LET'S GET STARTED

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