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Time to Ditch the Three-Legged Stool Analogy for Retirement and Replace it With a Two-Picture Analogy:
A Mailbox and a Piggy Bank

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At a very basic level, financing retirement is not much different than financing life. Strip away the verbiage we retirement professionals insert into the conversation, and it truly simplifies to a predictable stream of income and the spend down of the individual's retirement nest egg. Regardless of other motives we bring to the table, if the goal is to educate as many people as possible about preparing for and then paying for retirement, public policy should dictate we replace the proverbial three-legged stool of retirement—which might have suited us well for 80 years—with a down and dirty question: What income source in retirement will replace your salary while working?

Under this approach, the client, who is presumably still working and starting to think about retirement, is asked this question: Right now, your salary dictates your lifestyle, so when you stop working and retire, how much guaranteed income will you need to maintain your lifestyle? To this author, this is the only logical starting point. Individuals, regardless of socioeconomic status or educational level, should understand this conversation, and if they start to realize they will not have enough income, and not enough savings to purchase additional layers of income, they basically have two choices: work later than planned or downsize expectations of lifestyle. If we are having a live conversation with baby boomer clients, and advising and counseling them, this would be the appropriate time to quote Messrs. Richards and Jagger: "You can't always get what you want / But if you try sometimes, well, you just might find / You get what you need." Once an individual figures out ways to ensure a proper stream of income during retirement, every other asset owned by that individual will simply, by default, be called his or her nest egg, which will be liquidated to cover unbudgeted and non-recurring expenses. Any balance will be their legacy to family, friends and charities.

After understanding salary-replacement, possibly without ever hearing the word annuity, individuals can begin to envision some of the recurring retirement expenses for which they can draft a budget. They will soon realize expenses during retirement might be less than expenses while working, which justifies the historical emphasis by actuaries on pension replacement rates and the coordination with Social Security benefits, but they will realize they will need in the range of 75% to 90% of their current net take-home pay. Again, this is a great starting point because they are not passively listening to financial planners and attorneys talking over them, but are actively engaged in a conversation they fully understand.

Using a Stream of Fixed Income to Pay Living Expenses

Most of the following costs are controllable and can be reduced to appropriate levels with proper planning and time horizons. However, since out-of-pocket health care costs for Medicare, other than fixed monthly premiums and annual deductibles, are usually uncontrollable, they should be paid from the nest egg and not budgeted from the income stream. Typical expenses to consider (whether monthly, quarterly, biannually or annually) include:

1 This essay is loosely based on Barry Kozak, "ERISA Benefit Statements of the Future: The Need to Explain the Cost of Retirement, Including Out-Of-Pocket Medical and Long-Term Care Expenses," *Journal of Pension Planning & Compliance* 39, no. 1 (winter 2014); and Barry Kozak, "Qualified Retirement Planning Services to Your Clients: A New Fringe Benefit for Their Employees and a New Profit Center for You," *Benefits Law Journal* 29, no. 4 (winter 2016): 56.

- **For each home (primary, secondary or vacation):** mortgage or rental payments, property taxes, utilities, cable and phone bills, homeowners insurance, community assessment dues, alarm systems, landscaping and cleaning services, and other planned and expected maintenance costs
- **Taxes and fees:** federal and income taxes, state and local income taxes, sales taxes, renewal and licensing fees, and other required remittances
- **Debt:** credit card and other personal debt obligation payments
- **Automobile:** maintenance and tune ups, insurance and fees for parking passes, city stickers and disability vehicle placards
- **Insurance premiums:** life insurance, long-term care insurance, homeowners or rental insurance, and health insurance
- **Personal:** food, clothing and general personal upkeep
- **All other discretionary expenses that can be budgeted ahead of time:** vacations, hobbies, gifts, charitable contributions, dues for clubs and other organizations, securing professional services such as housekeepers, barbers, attorneys and accountants, and general entertainment

Here is where the individual planning for retirement should think of an image of a mailbox. A statement like "every month you are still alive, go to your mailbox and there will be a number of checks from different sources that, in the aggregate, will cover that month's budgeted expenses." Once this information is absorbed, we can add the complications of cost of living, joint life protection and all other risks that we, as professionals, can help our clients to mitigate.

The Spend Down of the Nest Egg for All Other Expenses

All other expenses that are unique, unbudgetable, unpredictable or, dare we say, unnecessary should be paid from the spend-down of the nest egg. This means that as long as the income stream is ample to pay all of the listed budgetable expenses, there should be no plan for the strategic liquidation of the nest egg (such as the 4% per year rule); rather, it should simply be ad hoc distributions as needed. Typical expenses to consider (whether periodic, random or contingent upon other events) include:

- Unexpected medical emergencies and other out-of-pocket health care expenses
- Retrofitting expenses in the home due to a disability and moving expenses if the current home cannot be retrofitted
- Assistance to a family member who is out of work, has a new baby, gets married, moves or goes to college, or other pleasant or emergency needs
- Large donations to charities or for funding of a legacy

As can be seen from this short list, the spend-down of the endowment could, and should, be used for some happy, pleasurable and positive expenses that were not budgeted, as well as expenses associated with emergencies. Here is where the individual planning for retirement should think of an image of a piggy bank. A statement like "every time you need extra money, dip into the piggy bank; every dollar remaining at your death will be your legacy passed along to your family, friends and charities."

Sources of Fixed Income

Now the individual planning for retirement sees that the most important aspect of retirement is the fixed income portion, and can develop a realistic budget; then we, as counselors and advisers, can explain sources of income, and if that is not enough, the priority of nest egg assets that should be converted into some form of income in advance of retirement. Most individuals are entitled to an annuity in the form of Old Age or Survivor benefits from Social Security, and although the monthly benefit depends on his or her compensation history and the number of quarters payroll taxes are contributed, each individual can choose a larger (actuarially equivalent, but don't use those words in front of your client) dollar amount by postponing the starting date. As to the employer retirement plans, if they have accrued benefits in a defined benefit plan, a discussion about opting for an annuity in lieu of a lump sum is very appropriate. If they have an account in a defined contribution plan, a discussion of taking the lump sum and converting it into an annuity stream (especially if the plan sponsor has adopted a qualified longevity annuity contract, or QLAC, option) is very appropriate.

Other general sources of annuities or income streams in retirement include (this is not an exhaustive list):

- Annuities and similar financial products from private insurance companies
- Corporate or municipal bonds that pay interest at specific points in time for a stated term
- Stocks that pay cash dividends
- Rental income
- Royalties
- Alimony and other family support payments
- Installment payments from damages awarded through lawsuits or settlements
- Sales of personal assets or businesses through an installment sale
- Certain long-term care insurance policies that provide monthly income to cover costs for assistance with activities of daily living
- Financial assistance from a governmental welfare program (i.e., Supplemental Security Income, Medicaid being called upon to pay the out-of-pocket costs associated with Medicare, Supplemental Nutrition Assistance Program, housing support)
- Reverse mortgages with an income stream
- Grantor trusts with an income stream (including charitable trusts)

Sources of Discretionary Income

This part of the conversation can end with a discussion of all other property owned by the individual that, by default, is part of the nest egg. A lump sum distribution from an employer-sponsored retirement plan can be rolled over into an IRA or deposited into some other form of savings or investment account (but the client must, at this point, also be taught about income tax issues with distributions, and instructed on required minimum distributions, which can upset any planned decumulation and spend-down phase).

Other general sources of discretionary income in retirement include (this is not an exhaustive list):

- Withdrawals from bank accounts or investment accounts (there might be fees for trades and premature liquidation)
- Reverse mortgages or home equity loans that provide withdrawals as needed or a source of credit
- Grantor trusts with a discretionary distribution option
- Monetary awards from litigation
- Gambling winnings
- The sale of property, a business or other personal assets
- The return of principal after the term of a corporate or municipal bond has expired
- Distributions from previously established health savings accounts
- Financial gifts and support from family and friends
- Financial gifts and support from charities, societies or other organizations
- Loans from, or viatical agreements against, life insurance policies

With a building block approach to education, the individual planning for retirement first envisions a mailbox, thinks about how fixed income during retirement will be the direct substitute for compensation while working, develops a budget with expected fixed living expenses, compares the realistic income stream with the expected budget, and then determines if there will be enough checks in the mailbox to pay his or her bills. If there are, great, but if not, they need to determine if there are any assets within the nest egg that can be converted into the missing part of the required income stream, if they realistically can continue working beyond the anticipated retirement age, or if they must now make plans to downsize the expected lifestyle in retirement to match the actual income stream.

Who is Responsible for Providing Financial Wellness?

Which actors should be providing this education and information about financial literacy and planning for retirement? Public policy suggests Congress should enact a law that requires a joint publication prepared and updated annually by the various federal agencies which can provide basic information about retirement, aging, end-of-life, estate and legacy issues, and links to their respective websites with more comprehensive information. Those agencies would likely be the departments of Labor, Treasury, Health and Human Services, Housing and Urban Development, and Veterans Affairs, and other tangential agencies, like Commerce, Transportation, Energy and even Homeland Security (for immigration or ex-patriot issues), and obviously some doctrinal input by the Department of Education. This will be the default notice that addresses the most common risks in retirement (why not suggest they start with the Society of Actuary's report and subsequent publications on this subject?). Such educational materials will ultimately be distributed to employers through the Department of Labor (DOL), so all members of the workforce will receive it.

This basic publication will be very generic, will provide the education discussed earlier, and will provide a more detailed summary of the various federal government programs generally geared toward retirees and older individuals:

- Old Age, Survivor and Disability benefits that will be paid from Social Security, and a basic education on timing choices
- Medical care costs that will be covered under the four parts of Medicare, and the associated out-of-pocket costs (most individuals have no idea that the portion of payroll taxes diverted to Medicare only cover the premiums for Part A, and that the individual must pay all other premiums, deductibles and co-pays out-of-pocket, or, if indigent, welfare, in the form of Medicaid, can be applied for to pay those other costs)
- A general discussion of long-term care, how it differs from medical care, and realistic costs for nursing homes and in-home care
- Aid and attendance benefits available for veterans with a disability

This new law, if enacted by Congress, can require the DOL to develop an additional model notice for employers that sponsor retirement plans. This notice can combine various communications already under their jurisdiction, such as a hypothetical disclosure of relative values, even in a defined contribution plan; whether or not it provides for any conversions to annuities (like a QLAC); and IRC § 402(f) Notice (which is under Treasury's jurisdiction). In this way, individuals can understand income tax issues well in advance of actual decisions and receive communications about their actual retirement benefits.

For employers who want to provide additional education as an employee benefit, Congress gave us a fringe benefit in the Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001 called "qualified retirement planning services." All we know from the statute is that employers who maintain a qualified plan can provide such education to their employees and their spouses, as long as the advice is available to non-highly compensated employees on a non-discriminatory manner. Since there is scant guidance under IRC §§ 132(a)(7) and 132(m) about what constitutes qualified retirement planning services, it is up to employee benefit plan consultants, together with other disciplines, such as social workers, dementia-care nurses, geriatric doctors, in-home medical and long-term care providers, grief counselors, funeral planners, estate planning attorneys, financial services professionals, speech therapists and all other professional disciplines that educate, support and advocate for people as they retire and age, to collectively develop the landscape of qualified retirement planning services.

Conclusion

This article suggests that we, in the industry, complicate the retirement planning discussion and then wonder why individuals have a glazed-eye look. Individuals of all socioeconomic and educational levels understand that while working, the paycheck covers monthly bills, and all other assets (whether cash in the bank, a line of credit or the sale of grandma's engagement ring) can be used to cover emergency expenses. Bankruptcy is the option when all else fails. Similarly, in retirement, the aggregate income stream replaces the paycheck to cover monthly bills, and the nest egg is spent down to cover all emergency expenses. Welfare and other programs specifically for the elderly are the option when all else fails. Congress should enact a law that requires model educational materials be prepared with input from all relevant federal agencies, and employers who want to provide a higher level of financial wellness should embrace those employee benefits professionals who provide "qualified retirement planning services" as a fringe benefit.

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