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POLL



Which of the following best describes the effect that the financial crisis has had on your personal work situation?

None, I'm as busy as ever

Changed my level of responsibility in same job

Substantively changed my job (e.g. my focus shifted to investments)

I'm considering a career change

I lost my job

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PERSPECTIVES FROM ANNA–FINANCIAL LITERACY

By Anna Rappaport

Financial illiteracy has been identified as a major obstacle to effective retirement planning for Americans. The SOA's Committee on Post Retirement Needs and Risks has spotlighted financial literacy problems and has repeatedly found misunderstandings and gaps in knowledge necessary for addressing post retirement issues. Two key recurring issues for individuals planning their retirement are a lack of long term thinking and a failure to understand and manage risks.

This article provides ideas to help actuaries think about ways to raise individuals' consciousness in these and other challenging areas. And for those who look at the work of the *Actuarial Foundation* and *WISER* and like what they see, I ask that you lend your support to these organizations. ¹

I learned a lot about the general topic of financial literacy from two sources: The 2008 Annual Report of the *President's Advisory Council on Financial Literacy* and *Nudge: Improving Decisions about Health, Wealth and Happiness* by Thaler and Sunstein.

What I learned from the President's Advisory Council Report This report included many insights into the issues and who is addressing various aspects of those issues. It includes a wide range of topics and provides a definition of "financial literacy." The council asserts that any individual completing a "comprehensive financial literacy program" should have an understanding of the following skills and concepts:

- "The capital market system and financial institutions;
- the participant's household's cash flow situation, and how to develop and maintain positive cash flow;

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- how to develop a spending plan that is consistent with their resources and priorities;
- the reasons for having an emergency fund and how to establish an emergency fund;
- the fundamentals of credit granting, including how to evaluate, select, and manage credit, and how to maintain a good credit rating;
- the process of deciding when to rent and when to buy a home, and the process of home ownership;
- the process of identifying various financial risks, including development of a risk management strategy to decide which risks they should take on and which should be transferred to an insurance provider;
- how to identify and protect themselves from identity theft and various financial frauds, and what to know and do if they think they have been victimized;
- basic investment products, the relationship between risk and return, and the what, when and why of choosing the best investments at the right time in their life;
- how to evaluate and take advantage of employee benefits and tax advantaged savings accounts;
- the various components of retirement planning, and how to develop an appropriate plan for a secure retirement; and
- how to develop a plan to assure financial security in the case of unexpected loss of income (disability or death) for those who depend on their earning power, and to assure the smooth transfer of assets to appropriate heirs."

This is an ambitious list, but it is encouraging to see a federally sponsored group look comprehensively at the components of financial literacy, how to teach it in the schools, qualifications of teachers, workplace topics, etc.

I was also very interested in a comment on worker's reactions to the information available and on the impact of financial literacy education on employers (from page 23 of the report):

"Surveys consistently find that the public feels overwhelmed and intimidated by the volume of financial information in the

marketplace. The result is paralysis—inaction, rather than action. However, employees appreciate receiving financial education in the workplace because they view their employer as a trusted source, and because instruction is convenient and accessible. In return, a financially literate workforce is likely to be happier, more focused and productive, and to have learned skills they can apply to their jobs."

What I learned from ***Nudge: Improving Decisions About Health, Wealth and Happiness***

My biggest learning from *Nudge* was that people make decisions around retirement planning as part of a much bigger picture—the same approach that drives decision making in many other areas of life.

I also learned from *Nudge* more about choice architecture and how important "framing" of decisions is. *Nudge* told me that "A choice architect has the responsibility for organizing the context in which people make decisions."

Putting It All Together

My view of the world as it relates to financial literacy, retirement planning and personal risk management could be described as follows:

General Topics

- The United States has problems with financial literacy. Well documented symptoms include low levels of savings and questionable retirement decision making. More will be known as The Financial Industry Regulatory Authority (FINRA)² is already conducting a major National Financial Capability Survey according to the President's Advisory Council on Financial Literacy report. The SOA's 2009 Survey of Post Retirement Risks, slated for release later this year, will provide more data, and the 2010 Pension Research Council symposium will be focusing on financial literacy.
- Actuaries have been addressing some of these issues through the Actuarial Foundation. Consumer education projects address specific gaps in knowledge, and youth education programs promote math literacy and the beginnings of financial literacy. The Actuarial Foundation also offers a high school level financial literacy program that includes workbooks for students and instructional materials for teachers.
- Many organizations, such as government agencies, not for profits and financial service companies provide literature, websites and

tools to the public, to employee benefit sponsors, and directly to employers for their employees. Much of this information is available at no cost on the Internet. Mymoney.gov is an excellent Web site with a wide range of financial literacy resources, including links to other government sites, such as Social Security and the Department of Labor. The Extension Service of the Department of Agriculture also offers a [site on personal finance](#), which in turn contains a [link](#) to additional tools from government and private sources. The [American Savings Education Council \(ASEC\)](#) and other organizations also offer quick paths to further information and resources.

Specific Population Segments

- For Americans in mid life and nearing retirement age, the Department of Labor's [*Taking the Mystery Out of Retirement Planning*](#) is a very good resource.
- The issues confronting lower and lower middle income populations are quite different from those confronting higher net worth populations, and they are generally not about investments. Two such issues are when to claim Social Security and retire, and how to manage housing and housing wealth. A new monograph from the SOA Committee on Post Retirement Needs and Risks will include a collection of papers on housing wealth and retirement.
- The "unbanked" have a very special set of problems. According to the President's Advisory Council report on Financial Literacy, there are nearly 73 million Americans who are either unbanked or "underbanked." To me, it is unrealistic to think about any kind of retirement savings or modern financial management program for them until they have access to mainstream banking and financial services.

Summary of Resources

- There is a large community of financial advisors but they largely serve higher net worth individuals—not lower income or lower middle income persons. Further, it can be debated whether they serve the middle class well
- Some not for profits provide advice and other services to the very poor, but the lower middle income group gets little hands on advice. They do not have money to pay for it and those who would provide it are not well tuned to their issues. Many people at all

levels do not seek advice and are suspicious of advisors.

- For Americans with computer skills but no computer, many public libraries offer free access to computers and the Internet. Some offer educational programs on topics like financial management.
- Other groups—such as the Women's Institute for a Secure Retirement (WISER)—provide financial education targeted at lower and lower middle income Americans.
- Some employers have worked very hard at educating their employees and structuring plans to enhance financial security, often with good success. The Profit Sharing Council of America Signature Awards contest identifies success stories, and there is a lot that can be learned from them. Plan structure can be more important than education, but both count. There are other contests and awards for good employee communication and other programs.
- One of the best ways to influence people is through an entity with whom they already have contact and whom they trust, for example, Social Security, employers, extension services and personal banks. All offer points of contact and build on existing relationships, and most offer leverage opportunities and have Web sites. Associations such as *SHRM*, *ABC*, *InFRE* and *ERIC* offer resources to employers and the opportunity to reach groups of human resource professionals at their meetings.
- Math illiteracy is a huge problem to which government programs commit significant resources. Those concerned about the long term future need to hope that some of this works. This is why the Actuarial Foundation places a major emphasis on math education.

The link between financial literacy and financial security. Financial security can come from specific group programs and from individual actions and choices. Even Social Security requires a decision about when to retire to make it work well. Employer sponsored defined benefit (DB) plans require decisions about when to retire and what option to use for payment of benefits. Employer sponsored 401(k) plans and many other defined contributions (DC) plans require decisions on whether (and how much) to save, investment choices, when to retire and when and how to draw benefits. For those who aren't covered by employer programs, financial security beyond Social Security is up to the individual. The best programs minimize the need for individuals to make too many decisions, but a certain degree of financial literacy is still required for those decisions to be sound.

Who Should Try to Improve Financial Literacy, and How?

Many groups are involved in this effort, and the President's Advisory Council report identifies some of them, including government, the educational system, not for profits, employers, and financial services companies. Actuaries have been involved through the work many of us do with clients and employers, through the research of the Committee on Post Retirement Needs and Risks, through the consumer education and math literacy efforts of the Actuarial Foundation, and through the work that individuals do in our local communities.

Leverage Resources: There is more to do. Identifying "low hanging fruit" methods of adding value at little cost and effort is a good first step for all. Regardless of what stakeholder I represented, I would try to leverage and get maximum benefit from what is already there, particularly from trusted governmental and independent not for profits sources. The discussion above lists some examples of available resources.

Connecting people and resources: One of the big challenges is how to connect to credible sources with credible information. If I were focused on finding a way to reach lower and lower middle income people, I would work through those who are already in touch with them. There is a need to both encourage better financial behaviors and provide assistance when needed. Organizations that might offer help to those who do not get help from employers or who want added help include the above mentioned Women's Institute for a Secure Retirement (WISER), Extension Service (linked to the U.S. Department of Agriculture), the Social Security Administration, American Savings Education Council, AARP, community and church groups, and public schools and libraries.

What is reliable? Another challenge is to help people sort out what is reliable information. An organization that wanted to do so could use a small group of experts to help vet submitted materials and then put a "seal of accuracy" on them. The sponsor would need a set of standards and guidelines on who could submit materials for the "seal of accuracy." The sponsor could also provide links to these materials on a Web site. One of the recommendations of the President's Council on Literacy is to establish a "Workplace Financial Literacy Honor Role." The Profit Sharing Council of America's Signature Awards are another variation on this theme.

Tailored advice for lower income people: Here is another idea that could work at moderate cost. There are not for profits who offer various kinds of advice to people who are not served well in the marketplace. I don't know how many give financial advice, but there are certainly models that could be extended, and probably existing groups that could be built on. In Chicago, for example, there is an elder law clinic connected to a local university. If you come in with a problem and do not

have money, they provide service at no cost. If you have money, they help you to identify the type of service you need, and redirect you to the appropriate marketplace resources. Many not for profits have severe financial problems of their own today. Very modest grants or hands on help to some of them might well get advice to a large number of underserved Americans.

Conclusion: Financial literacy is a big and complex topic, and is interwoven with success in achieving financial security. There are a lot of resources to help people who are interested, but there are still many gaps in knowledge and problems connecting those who need the advice with those who can provide it. The topic of financial literacy offers both a challenge and an opportunity for actuaries as they work with clients, perform public service (including with the Actuarial Foundation), and as they deal with their own lives and those of their families and communities. This topic offers us a great chance to think about the question: "How can I make the world a better, more financially secure place?"

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¹ A personal disclosure is in order. I serve on the WISER Board and am a Trustee Emeritus of the Actuarial Foundation and a member of the Consumer Education Committee.

²The Financial Industry Regulatory Authority (FINRA) is the largest independent regulator for all securities firms doing business in the United States. All told, FINRA oversees nearly 4,850 brokerage firms, about 173,000 branch offices and approximately 649,000 registered securities representatives.

Created in July 2007 through the consolidation of NASD and the member regulation, enforcement and arbitration functions of the New York Stock Exchange, FINRA is dedicated to investor protection and market integrity through effective and efficient regulation and complementary compliance and technology-based services.

