THE 401(K) AND SOCIAL SECURITY MYTH

"Is there a better, more secure and predictable way to plan for retirement?"

"We'll review the pitfalls of the current "system" you may not have known about, and discuss a solution".

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Financial Planning
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An Independent Fiduciary Registered Investment Advisory Firm

HOW THE 401(K) WAS CREATED

You may think that the 401(k) employer-sponsored retirement savings plan was a carefully crafted plan, created by our beloved congress to help citizens save for their eventual retirement. NOPE!

As a result of pressure by the public to reform pension abuse in the 1970's. Employers were now required to accept more responsibility of the management of their pension fund and could now be sued for mismanagement of their fund. As a result, the 401(k) morphed into a way for employers to transfer the responsibility of saving for retirement onto their employees.

Ted Benna, an employee benefits consultant, was the first to exploit the 401(k) section of the new ERISA code to help highly compensated employees save more of their earnings. He never imagined that the 401(k) would replace pensions and become the primary vehicle that so many Americans would use to save for retirement. He, along with other early promoters of the 401(k), originally envisioned it as a **supplement** to company pensions.

Again, the 401(k) was never intended by its creators to be a workers' primary means of income replacement in retirement.

And, under the IRS code, the plan had to be available to all workers under the plan, not just the highly compensated. Companies began closing their pensions funds and transitioning their employees into a self-directed 401(k) plan, where the lower-level employees had no experience or training on how to 'self-direct' their savings, and no requirement to participate. Many employees didn't contribute enough, or sadly some employees didn't contribute anything at all. Employees need lots of help and guidance, and even mandatory participation, but none of these are required for 401(k) plans.

By age 55, you should have at least seven times your salary saved.

Source: T Rowe Price

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Jay Clayton – Chairman
Securities and Exchange Commission

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WHAT'S THE PROBLEM WITH 401(K) PLANS?

401(k) plans were not set-up to replace pensions. A pension is designed so that a guaranteed monthly amount is paid to a worker, once they leave the workforce, and the pensions payments are to be paid for the rest of the retired workers lifetime.

The traditional pension was funded primarily by the employer, not the employee. Now, very few employers currently offer pensions.

PENSIONS VERSUS 401(K) PLANS

Government employees and union employees have the best pension plans. People in the private sector have an array of good or not-so-good 401(k) plans or no plan at all. For all private businesses in the U.S.A, only 50% of all workers have access to a defined contribution – 401(k) plan, through their employer.

Benefits of Pensions

A pension is a better safety net than a 401(k) plan. The employee knows the amount of the monthly payment he/she will receive in "retirement".

A pension is set-up and overseen by investment professionals. The pension assumes the investment risk, not the employee.

Investment choices are selected by investment professionals.

The pension plan is protected by insurance if the employer goes bankrupt or the investments choices are not sufficient to fund the payments.

DRAWBACKS OF A 401(K) PLAN

It is very helpful to have a retirement savings plan with an employer match as a workplace benefit. I believe we can do a much better job to put safeguards in place to improve the success of each 401(k) plan or any other type of plan.

DRAWBACKS OF A 401(K) PLAN

- **The responsibility of saving and investing is the sole responsibility of the employee**. An employee is not required to save for retirement. However, some employer have implemented automatic opting- in. Meaning the employee is automatically enrolled in the plan. The employee would have to "opt-out" to stop contributions going into their 401(k) account. This opt-in feature has increased employee participation.
- **Employees receive little guidance from their employer or from the investment advisor selected to oversee the 401(k) plan.** As defined in the rules of the plan, a 401(k) plan is "self-directed", meaning the employee 'directs' their own plan. The employee selects the mutual fund(s) he/she is going to invest in and the employee decides how much of their pre-tax salary they are going to save in the plan.
- **Employee ability and knowledge**: Most employees are not trained investment professionals, so they are not equipped to take on the responsibility of managing the most important investment account they will probably have in their lifetime.
- **Employees are allowed to take loans from their 401(k) plans**. Taking a loan from your 401(k) plan hurts your progress if you take a long time to repay the loan. All the time the money is not in the 401(k) plan you are missing out on any appreciation in value of the account and dividend payments which are then reinvested and able to appreciate in value as well. Of course, in an emergency you may have no other choice. You can "loan" yourself up to $50,000 or 50% of your 401(k)-account balance, whichever is the lower amount. You are required to pay yourself interest on the 'loan". The interest is deposited back into your 401(k) account. But, one bad thing is, the interest you are paying yourself is after-tax money (that money has already been taxed). When you eventually withdrawal that money from your 401(k), it is taxed again. Double taxation of 401(k) loan interest becomes a meaningful cost when large amounts are borrowed and then repaid over multi-year periods. The loan *can* be a lower cost alternative means of accessing similar amounts of cash through bank/consumer loans or stopping the deposits into your plan for a **short time.** If you don't pay back the loan as scheduled, the money will then be considered table income by the IRS and you will be required to pay ordinary income tax on the funds.
- **401(k) plans have no guarantees**. Unlike a pension, a 401(k) plan has no built-in guarantee. It's completely up to the employee how well their plan might do. Even if the employee tries to do everything right, they may end up with a final balance that is insufficient to fund their retirement for the rest of their life.

Drawbacks of a 401(k) Plan, continued…

- **FEES: 401(k) plan participants are at the mercy of mutual fund companies.** Mutual fund companies have had a monopoly on 401(k) plans since their creation in 1980. What happens when you have a monopoly? You have high fees. Only recently have retirement account fees come under scrutiny from regulators and because of the benefit of easily finding information on the internet. People are getting wise to excessive fees. In addition to mutual fund fees, costs to administer the plan are most often paid by the plan participants (the employees). If an employee did not have an employer match, it could be less expensive for an employee set-up their own individual retirement account and pay a financial advisor to manage their account. It's an option every employee should look into. It could save you thousands. See table 1 below:

TABLE 1.

Company managing your 401(k) Plan versus Individual retirement account (IRA) managed by Financial Advisor	Range of Fees and expenses associated with a 401(k) Plan versus Individual Retirement Account
Mutual Fund Fees: 12-B1 fee, sales charges, annual service charge, withdraw before maturity charge,	0.1% to 3.5%
Plan Administration Fees: annual fees, one-time fees, transaction fees	0.1% to 2.5%
Your 401(k) fees at employer =	**0.2% to 5.0%**
Financial Advisor Fee to manage an IRA	0.25% to 1.25%
Financial Advisor selected funds/investments fees: range of fund fees for best performing ETF's & Mutual Funds for IRA *	0.0 % to 0.05%
Plan Administration Fees for an IRA	$12 annual account fee Pershing Bank of NY
Your IRA fees with financial advisor =	**0.0% to 1.30% + $12 annual acct. fee**

* Financial Advisors get preferential pricing.
They have access to lower priced fund share classes, that are not available to the public and have access to the full array of investments. If you work with a financial advisor, you will receive preferred pricing too.

Interesting Fact:
Institutional Share Class
This is the share class that is available only to financial professionals. It's fee (expense ratio) is always lower than an "A" share class, or any other share class.

The cost of 401(k) plan fees over a lifetime

A recent study found that the typical American worker who earns a median salary starting at age 25

will pay about $138,336 in 401(k) fees over their lifetime.

The cost is even greater for high-income earners. These figures are reflective of average 401(k) fees, which estimates to be approximately 1% + of total plan assets.

Another study found that 401(k) participants pay an average all-in fee of 2.22% of their assets, but that there is a wide range between 0.2% and 5% (Source: Center for American Progress)

There is a way to reduce 401(k) fees without sacrificing returns. As independent advisers, we can shop from a number of asset custodians, and also find the best funds that also have the lowest expense ratios.

A Fund Name	B Assets (as of 01/31/20)	C Total Expense Ratio (Net)	D Total Expense Ratio (Gross)	E 12b-1 Fees	F Sub-Transfer Agent/ Shareholder Servicing Fees	G Common Collective Trust Service Payments	H Total Paid to ADP
State Street Cash Series US Government Fund - Class L	$27,167.84	0.75%	0.75%	0.00%	0.00%	0.68%	0.68%
PIMCO Total Return Fund - Class A	$1,294.98	1.05%	1.05%	0.25%	0.20%	0.00%	0.45%
DWS Global High Income Fund - Class S	$13,052.24	0.65%	0.76%	0.00%	0.25%	0.00%	0.25%
State Street Aggressive Strategic Balanced Sec Lending Series - Class VII	$3,020.66	0.87%	0.89%	0.00%	0.00%	0.78%	0.78%
State Street Conservative Strategic Balanced Sec Lending Series - Class VII	$111,771.57	0.87%	0.91%	0.00%	0.00%	0.78%	0.78%
State Street Moderate Strategic Balanced Sec Lending Series Fund - Cl VII	$119,312.07	0.87%	0.89%	0.00%	0.00%	0.78%	0.78%
AB Relative Value Fund - Class A	$196.89	0.90%	0.99%	0.25%	0.25%	0.00%	0.50%
DWS CROCI U.S. Fund - Class A	$488.85	0.99%	0.99%	0.25%	0.35%	0.00%	0.60%
Franklin Rising Dividends Fund - Class A	$8,809.37	0.87%	0.87%	0.25%	0.25%	0.00%	0.50%
State Street S&P 500 Index Securities Lending Series Fund - Class IX	$0.00	0.70%	0.70%	0.00%	0.00%	0.50%	0.50%

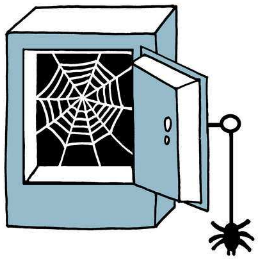
Revenue Sharing

Here's an example of a company's 401(k) plan statement. Revenue sharing is highlighted in red. What is revenue sharing? In this example, the plan administrator; ADP Company (you know, the company known for home alarms), is getting paid from the employee's funds in the plan. It's listed as a percentage of each fund. This is not a fair and transparent way to report expenses that employees are paying. Usually, employers or employees often don't realize the total cost. The revenue sharing is always charged as a percentage of plan assets. That means plan participants (employees) will automatically pay ADP higher and higher administration fees <u>for the same level of service</u> as their account grows. That's not fair, it's a rip-off!

IN THE YEAR

2035

Social Security will begin to run out of money



What will happen?

- Benefits will be cut
- Federal Gov. will borrow to pay benefits
- Age to get full benefit will be increased
- Payroll taxes to fund social security will increase
- Increase taxes on Social Security benefits
- Cut the cost of living (inflation) increases
- Increase required contribution rates

SOCIAL SECURITY IS IN TROUBLE

WHAT IS CONGRESS DOING?

Congress has known about projected Social Security short comings since 1972, and has kicked the can down the road, instead of coming up with a permanent solution. The tail-end of the Baby Boomer generation that is poised to begin taking benefits in the next few years, will be the first to bear the brunt of cuts to their benefits.

The bottom line is that you cannot expect to receive the full benefit you are entitled to.

Gen X and Millennials will pay more into social security than past generations, but receive less benefits.

Another strain to the Social Security fund is disability benefits. A record 5.4 million workers and their dependents signed up to collect federal disability checks when President Obama took office in 2009.
As a result, the swelling ranks of the disabled became a drag on the economy. A White House report noted that because "workers on SSDI rarely return to the labor force," this can result "in a loss to society of the economic contribution those workers could have made."
As of 2019, there are now 8,378,374 people receiving disability payments.

IT'S AN UNSUSTAINABLE PROGRAM

The Social Security system is now paying out more in total benefits than it collects in income.

Money has been borrowed repeatedly from the Social Security fund to keep disability insurance payments flowing.

A couple with average earnings turning 65 in 2010, would have paid $600,000 in taxes, but would collect just $579,000. Each year, this will get worse. You will pay a lot more into Social Security that you will collect.

By 2036, there will be almost twice as many older Americans as today — from 43.2 million today to 78.1 million.

Considering these facts, you need to prepare for the possibility that Social Security will not be there for you.

Source: ssa.gov, Investor's Business Daily

401(k) Traps

<u>Fails as a retirement strategy</u>

Was not designed to be the primary retirement account.

No stable returns.

No tax advantage: funds are taxed 100% at ordinary income tax rate, not the lower capital gains tax rate.

Your taxes will probably be higher, not lower, when your distributions are taxed.

Limited liquidity: Rules and penalties make accessing your funds difficult.

No guarantee: success is 100% dependent on you.

High fees & expenses

Social Security Traps

You pay more into Social Security than you receive in benefits; it's a net-loss game.

You will not know your final monthly benefit: Congress will make changes.

Disability Insurance is an out of control program that hurts Social Security participants.

Social Security income is subject to income tax.

WHAT YOU SHOULD DO*

Setting up and funding other investments is imperative to avoid the traps that 401(k)'s and Social Security presents. Unfortunately, even if you are self-employed, you cannot avoid paying the Social Security tax on your income.

- Evaluate your 401(k) plan at your workplace with the assistance of a fiduciary financial planner. Determine the employer match, fees and expenses you are paying, and if it makes sense to fund an individual retirement account.
- A detailed projection of your earning potential and tax liability in future earning years, should be performed to assess possible strategies.
- Do a detailed assessment of your income and expenses to see the opportunities to save more.
- Set-up a Roth IRA account, to invest your after-tax income.
- Evaluate funding other investments that will provide more reliable appreciation and later, provide a guaranteed income.
- Review your current estate planning documents to assure proper tax planning strategies are in place to optimize tax savings, now and in the future.
- Review your current plan to look for opportunities to assure liquidity for some investments.

* Note: this report is for informational purposes only and should not be taken as specific advice for your individual situation. Seek out the assistance of a registered financial planner to determine the right strategy for your situation. Qualified retirement accounts have many rules and restrictions to consider. Tax rules are known to change frequently. Consult a certified public account for specific tax rules for your situation.

You don't want the government involved in your finances for the rest of your life.

There is a better way to plan for retirement.

Next Steps

Questions that need answers

Review your plan for sources of predictable income and guaranteed income. Does your retirement plan have multiple sources of income? Or are you only relying on Social Security and your 401(k) plan? Is much of your net-worth invested in real estate?

Have you planned for inflation to erode your buying power? What model did you use to arrive at your expected inflation rate?

If you know you will have adequate income, how is it protected? Will all of your income in retirement be subject to taxation, if so, how much of your expected income will be lost to taxes?

Take Action

My hope is that you will seek out advice, get a second opinion on what you're currently doing. In my opinion, the "system" has failed a lot of people. While I won't re-hash what happened in 2002 and 2008 when the stock market experienced historic losses.

What I will ask is,

If you were going to retire in six months, and tomorrow, there was another economic crisis, and the stock market fell 47% in two months, would you be all right? Would your retirement portfolio be unaffected?

Contact our office now to learn about our process to protect and grow your assets.
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