

This “special report” focuses on retirement *income* planning as members indicated earlier in 2010 that retirement income distribution planning was their number 1 area of interest within the area of retirement planning.

# RETIREMENT INCOME PLANNING

## Planners Find Success with Retirement Income Strategies

Our introductory article frequently highlights findings from recent research. The remainder of the special report typically focuses on strategies or expert insights designed to help you take your practice to the next level.

by Carly Schulaka

**A**s America ages, clients are demanding more retirement income planning products and services, and planners are stepping up to meet that demand. Whether a planner's primary strategy for providing retirement income involves a systematic withdrawal, time-based segmentation, essential versus discretionary income, Social Security and pensions, or a combination of strategies, planners are generally successful at executing retirement income planning. They're keeping the majority of their clients in or near retirement from having to make any significant changes to their retirement plans or lifestyles, notwithstanding a lagging economy.

According to FPA's 2010 *Financial Adviser Retirement Planning Experiences, Strategies, and Recommendations Study*,

which queried 425 FPA members in September, 60 percent of planners' clients received retirement income products, services, or advice from them in the last 12 months, compared to 53 percent of planners' clients in 2009, according to similar research conducted last year.<sup>1</sup>

The increase in retirement income planning may simply be attributed to the fact that each year more baby boomers are closer to retirement. However, it may also be thanks to a shift in attitude.

"At the end of 2008 and early 2009,

we saw a lot of people who were just too shell shocked to do anything," says Michael E. Kitces, CFP®, CLU, ChFC, director of research at Pinnacle Advisory Group. He indicated that people are re-emerging from their shells, engaging planners, and seeking solutions, which would help account for the reported increase in retirement income planning.

### Success Across All Strategies

In 2010, planners report that 60 percent of their clients in or near retirement have made no significant changes to their retirement plans; this is the same finding as the 2009 survey.

The 2010 survey also shows that just 17 percent of planners' clients in or near retirement have had to delay their retirement date. This is significantly less than what has recently been reported in two consumer polls. A survey from consulting firm Towers Watson shows that 40 percent of U.S. workers plan to delay their retirement,<sup>2</sup> and similar research from Sun Life Financial shows 52 percent of U.S. workers expect to work at least three years longer than originally planned.<sup>3</sup>

Rebecca King, manager of the FPA Research Center, says FPA's 2010 retirement study continues to affirm the value of financial planning.

"We've seen this type of success in

other research as well, such as the 2008 *Value of Financial Planning* study, so we know that professional financial planning provides tangible benefits," says King. "The 2010 research shows that financial planning provides benefits in times of economic crisis as well as economic growth."

According to the 2010 survey, all retirement income strategies generate approximately the same level of success when measured by the financial and lifestyle changes clients in or near retirement have to make. (See Table 1 for details on the strategies.) However, the essential versus discretionary income strategy does correspond to a higher percentage of clients who have had to significantly adjust their lifestyles than all other strategies (read more about this on page 31).

As shown in Table 2, planners use a variety of products for retirement income planning purposes. Overall, planners are successfully helping clients in or near retirement maintain their lifestyle and retirement plans no matter which products they most often use.

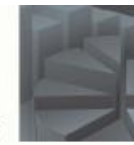
However, planners who are not making any product recommendations have the highest percentage of clients who have had to significantly adjust their lifestyle due to economic conditions.

"Planners who are not making any recommendations should take a close look

When relevant, we report on measures of success so you know how your client success levels compare to average for clients receiving professional advice. In addition, these findings can be shared with clients or prospective clients to highlight the tangible benefits of financial planning.

We conduct significance tests on findings so you can be sure we aren't simply reporting data anomalies. We then provide interpretations that are grounded in the data. In this case the data is comprised of two parts: 1) planners who do not use/recommend any products to their clients for retirement income planning purposes and 2) of those planners, what percent of their clients had to adjust their lifestyle due to economic conditions compared to the average percent of planner clients. The percents are: For those planners who do not make any recommendations, 46.25% (mean) of their clients in or near retirement had to significantly adjust their lifestyle compared to 19.55% (mean) of all planners' clients.

Get a snapshot view of how your practice compares to other practices, or future trends for you to plan for now, with this type of information.



When relevant, we make recommendations on metrics planners can examine to see if something merits further investigation. In this case we suggest that planners examine their client implementation rates if they don't recommend or use any retirement income products.

at the percentage of clients who are implementing the retirement plan," says King. "It's possible that their clients simply aren't getting these recommendations anywhere and, as a result, are not effectively saving or planning for retirement."

**Essential Versus Discretionary Income**

The 2010 study data show that among planners who primarily use an essential versus discretionary income approach, an average of 25 percent of their clients in or near retirement have had to significantly adjust their lifestyle in 2010—the highest percentage of any income strategy used.

This does not necessarily mean that the essential versus discretionary income approach is the least effective strategy for keeping retired clients on track; instead, it may point to the planner's ability to better identify when clients need to make changes.

For Jonathan T. Guyton, CFP®, principal of Cornerstone Wealth Advisors and author of influential research on safe withdrawal rates, the survey finding related to essential versus discretionary income may be a product of recency bias. Recency bias is the phenomenon of giving more weight to recent events than events that took place in the past.

He offers this example: A retired client with a \$1 million retirement nest egg has \$30,000 in essential expenses. Using the essential versus discretionary income approach, you may be interested in buying an annuity to guarantee \$30,000 of inflation-adjusted income, and you may need as much as \$800,000 or more of that \$1 million to do so. Because the essential income is locked down in "safe" things, you may be inclined to invest the remaining \$200,000 of discretionary funds more heavily—say 75 to 80 percent—in equities.

"Then you get a big downturn in 2008 and 2009, and most of that \$200,000 is in equities, so now you're down to around \$140,000 or \$150,000, and

**Table 1: Income Distribution Strategies Used**  
Which one of the following best describes the strategy you use most frequently to provide retirement income to your clients?

	2009	2010
<b>Structured systematic withdrawal program:</b> Diversify investments based on client's risk profile and manage the total return of the client's entire portfolio. To provide income, draw down a percentage of the portfolio periodically or withdraw interest and dividends only.	40%	50%
<b>Time-based segmentation approach:</b> Set up separate pools of investments with lowest-risk investments in the near-term time horizon segment, somewhat higher-risk investments in the next segment, and riskiest portfolio in the longest-term segment. Income is drawn from one segment at a time. Once the first segment is depleted, assets from the second segment are used for income.	32%	28%
<b>Essential versus discretionary income approach:</b> Classify client's retirement expenses as essential or discretionary. Low-risk investments or annuity guarantees are selected to fund the essential expenses. A mix of medium- and higher-risk investments is selected to fund the discretionary expenses. Income is drawn from both funds: one fund to cover essential expenses; the other fund for discretionary spending.	14%	14%
<b>Social Security and/or pension:</b> In most cases, do not use a structured portfolio or strategy to provide retirement income to clients. Clients mainly live on pensions and Social Security, which may be supplemented periodically.	7%	4%
Other (please specify)*	6%	5%

\*Other includes a combination of the above strategies and managed cash flow.  
Source: FPA's 2010 Financial Adviser Retirement Planning Experiences, Strategies, and Recommendations Study

Options that are not as frequently chosen are pulled out of the main table and included below so you can see the most applicable items at a glance.

**Table 2: Financial Products Used**  
Which of the following financial products do you use/recommend with your clients for retirement income planning purposes? (Select all that apply.)

Options	2010
Income and dividend-paying investments	86.60%
Bonds	71.10%
Long-term care insurance	67.50%
Treasuries/TIPS	54.60%
Exchange-traded funds (ETFs)	54.40%
Certificates of deposit (CDs)	52.40%
Single premium immediate annuities (SPIAs)	43.10%
Variable annuities with guaranteed living benefits (GMIBs, GMABs, GMWBs)	43.10%
Medi-gap insurance	33.12%
Fixed deferred annuities	25.90%
Reverse mortgages	16.00%
Other (please specify)*	10.60%
Target maturity funds	10.20%
Other variable annuities	9.60%
Other immediate annuities	9.40%
Long-term care annuities	8.20%
Managed payout funds (income replacement funds)	5.40%
None	0.90%

\*Other includes mutual funds, REITs, structured products, life insurance and limited partnerships  
Source: FPA's 2010 Financial Adviser Retirement Planning Experiences, Strategies, and Recommendations Study

We explore categories as well as specific types of products so you can see more clearly how your product mix compares to your peers.



**The Business Benefits of Retirement Planning**

Planners attribute some new client acquisition to the fact that they provide retirement planning services, and that amount of new business is growing.

In FPA's 2010 *Financial Adviser Retirement Planning Experiences, Strategies, and Recommendations Study*, nearly 25 percent of planners indicate that more than 10 new clients had come to them for retirement planning services in the past 12 months, up from 17 percent in 2009.

Planners who have retirement income planning expertise are also consolidating more assets from current clients. In the 2010 study, planners indicate that 60 percent of clients who have received retirement income products, services, or advice from them have since consolidated more assets with their firm; that's up from the 48 percent of clients who consolidated more assets in 2009.

"I think advisers are starting to realize that if they don't take an offensive position in terms of retirement income management and planning, they are at risk of losing those clients," says Kevin S. Seibert, CFP®, CRC®, CEBS, principal at InFRE Retirement Resource Center. "We know from research that clients have a higher probability of changing advisers 5 to 10 years prior to retirement. If they're not confident that their current adviser is the one who can do [retirement income planning] for them, they will find someone who can."

the client goes, 'Holy cow, a quarter of the money in my discretionary fund is gone!' explains Guyton. "They fail to see that their planner has actually kept 20 or 25 percent in fixed investments, but they do see the large percent decrease in their discretionary pool, and they start to connect some dots that say, 'I have to significantly reduce my spending,' and that leads to a bigger percentage of people doing just that.

"Ironically, the very approach that was meant to stabilize retirement income in the face of economic fluctuations has—according to your research—actually produced greater volatility in retirement income, and that's a product of recency bias."

**Sustainable Withdrawal Rate on the Rise**

Planners who most commonly use a structured systematic withdrawal program were asked to indicate what they usually recommend as a sustainable withdrawal amount. In 2009 the average rate was 4.4 percent. In 2010,

the average rate is 4.75 percent.

Kitces admits that it's difficult to know what the source of that increase is, but he says it could be a result of the growing body of knowledge indicating that a 4.0 percent withdrawal rate with no other adjustments may be too low.

"I think it recognizes a growing base of research that says that for some clients, in some situations, taking a higher rate than a flat 4 percent is okay," says Kitces.

Guyton agrees, saying planners have become more familiar with research by Kitces suggesting that in a lower market valuation environment, the withdrawal rate that is sustainable is higher; the converse is also true. Planners may also be more familiar with research Guyton has conducted suggesting that if clients are willing to make some small adjustments, then the safe withdrawal rate can be about a full percentage point higher than if they are not willing to be flexible.

But if planners are increasing withdrawal rates because they feel things are better in 2010 than they

were in 2008 or early 2009, that's counter-intuitive to what the research shows, according to Guyton.

"It may be tempting to think that when the market is at an all-time high maybe you can take out 6 percent or more, and if it's really low you should only take 4 percent—but that is a 180-degree difference from what the research demonstrates," he says. "In a way, though, that's what human behavior suggests. In fact, even though the withdrawal amount may be slightly reduced in extreme down markets, the safe withdrawal percentage could actually be higher."

Guyton offers this example: A client with \$1 million is doing a systematic withdrawal, taking out \$50,000 a year, or 5 percent. The market drops dramatically, and the \$1 million goes to \$700,000, so you tell the client he should reduce what he's taking by 10 percent (\$50,000 becomes \$45,000). Now you have \$45,000 of \$700,000, which is about 6.4 percent.

"Your withdrawal rate has gone up and your withdrawal amount has gone down, and that flexibility, that small reduction, is exactly what you should have done in a market that is very lowly valued," he says.



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**Endnotes**

1. FPA's 2009 *Financial Advisers' Attitudes and Perceptions About the Retirement Income Distribution Market Study*, conducted by Diversified Services Group and sponsored by Nationwide Financial.
2. Towers Watson study of 9,100 employees conducted in May and June 2010: [www.towerswatson.com/press/2919](http://www.towerswatson.com/press/2919).
3. Sun Life Financial Inc.'s *Unretirement*<sup>SM</sup> Index, October 19, 2010. [www.sunlife.com/us](http://www.sunlife.com/us).

Industry statistics like these can be used to help shape your business plan or strategy. They can also be used to benchmark your practice against the average practice to see where you have growth opportunities or areas where you are already experiencing above-average success.



When our research identifies a change or issue that it cannot effectively address, we bring in experts to provide insights based on their experience and knowledge.