Opinion: This is why modern retirement planning doesn't work

By Thomas O'Connell

The truth about retirement planning and your family legacy

If the things you thought to be true weren't, when would you want to know?

Let's think about the theories and myths that make up "traditional retirement planning." We have:

1. Modern Portfolio Theory (Asset Allocation) – 65-years-Old – Doesn't work – "Investing in the 'Slow Growth Forever' Global Economy: Overcoming the Common Wisdom" by Kirk Spano, Nov. 21, 2016, FunamentalTrends.com.

2. 401(k)s – 30-years-old – Doesn't work – "The State of American Retirement: How 40(k)s have failed most American workers" by Monique Morrissey, March 3, 2016, Economic Policy Institute.

3. IRAs – 40-years-old – Doesn't work – Same as No. 2.

4. 4% Rule – 20-years- old – Doesn't work - "The 4% Rule is Not Safe in a Low Yield World" by Michael Finke, Wade Pfau & David Blanchett, Journal of Financial Planning, 2013.

5. Average Rate of Return – Ancient – Not only not true but irrelevant as well – "Solving the Myth of Rate of Return" by Erik Krom, Fox Business Online, April 30, 2012.

There are others of course, but these are the leading ones that are pounded into our heads. If these theories were true or worked then why do we have a retirement catastrophe on our hands right now? If investing were a science as everyone tries to lead you to believe, then nobody would ever lose money. Every study out there — whether from Fidelity, Pew, whomever — reveals that the leading concern retirees and pre-retirees have by an overwhelming majority is "Will I run out of money in retirement?"

If modern retirement planning actually worked, only a small minority of people would be concerned about running out of money in retirement.

The "traditional retirement planning" theory is dead.

R.I.P.

Worse than the plight of soon-to-be retirees and current retirees is the prospects for the next generations, yes plural. They'll be saddled with trillions of dollars in student loans. They will inherit $20 trillion in national debt which is estimated to be at least $30 trillion by the time they start to retire. Personal income tax confiscation is estimated to go up by over 30% in the next five years according to the Congressional Budget Office (CBO).

Anemic economic growth that has plagued us for the last 10 years is likely to remain with us for another 10 years, or longer. They'll need to care for aging parents as they try to raise and educate their own families. With all these headwinds, how will it be possible for the children and grandchildren of today's retirees to accumulate any kind of wealth to put their kids through college, let alone save for their retirement? The sad answer is that except for a lucky few, most can't and won't. And this outlook is likely to worsen, not improve, for the generations that follow.

When we get married, we sit at the kitchen table and talk about our goals and dreams for the future. Then the kids come along, and we sit at the kitchen table and put some of our goals and dreams aside and talk about the hopes and dreams we have for our children. Rarely in that discussion do we talk about how our children might pay off insurmountable debts, pay for our nursing home or how they may never be able to retire.

Our goal, like that of our parents and grandparents before us, is that our children and grandchildren will be a little better off than we were, and that this family legacy will continue to get passed from generation to generation. Unfortunately, we may not be able to leave behind a better world for our children, as our parents did, especially if we continue listening to bad advice and failed theories about traditional retirement planning.

Don't you find it ironic, especially with all of today's headlines talking about fiduciary responsibility, that many of the media "experts and pundits" who continue to espouse these failed theories on their television and radio shows are not even licensed to do so? They have absolutely no fiduciary responsibility with respect to the bad advice they give you. Why are they continually given a platform when they are so often wrong?

Since many of today's pre-retirees and retirees aren't in a position to financially help their children and grandchildren, what if, by planning together with your children, you discovered an opportunity to create millions of dollars, guaranteed and income tax free for your family? Would you take it? What if as a last act of love, you could leverage your time left here for their benefit? Time might just be the most valuable asset you have that they can use.

Pretend your son or daughter listened to the same failed theories. They diligently save in their government sponsored retirement plans – let's say in this example a 401(k) plan. For the next 25 years, they set aside $15,000 each year, and at the end of that time they'd have $375,000 in contributions. Now let's imagine they earned a real rate of return of 4% per year, which according to DALBAR (an independent research group that provides this information on a yearly basis) is higher than the average investor has earned as a real return in the last 25 years. They'd have a pot of approximately $650,000 (actually $649,676). Keep in mind though, the maximum they would have available to use is $50,000 via a loan mechanism, unless of course they were willing to pay taxes and maybe an extra early distribution penalty if they were under 59½. But wait, that $650,000 isn't all theirs. The government needs to get its share. Since no tax has been paid on it yet; the government sponsored retirement plan only allowed them to postpone paying taxes. If today's tax rates hold steady into the future (which we already know will actually increase), your son or daughter will owe the government between 20-40% of that $650,000. And I haven't even considered inflation. So if this is their main pool of assets for retirement survival, truthfully, how could we ever expect them to make it?

As an alternative, pretend now that instead of contributing money into a government sponsored retirement plan, your son or daughter took that same $15,000 and was able to leverage that by a multiple of 5, 10 or even 20 times. In a worst-case scenario they would be guaranteed a minimum of $650,000, and maybe even as high as $1 or $2 million, before or at the 25-year mark, but now the $650,000 they receive is income-tax free. And they'd have control and use of 70% to 90% of their contributions and earnings along the way also tax free. How much would you encourage your children to put in a plan like this? Best of all, it doesn't cost you, mom and dad, any money out of your pocket, though you could contribute if you were able to.

So what is this solution? There are three parts to this answer; 1) control, 2) leverage and 3) the contract. The key to all this is to consider the family as an investment. In Leonard Renier's book "The Family Legacy: The Generational Solution," he discusses exactly what all the wealthy families around the world do. The shame of it all is that this type of planning is available to every family in America, but has never been taught to us. For a historical perspective read about the different paths the Rothschild and Vanderbilt families took and where those two families are today. Early on the Rothschild family created a 'family banking' system which included the use of life insurance and parlayed that into being one of the richest families in the world today. The Vanderbilt family on the other hand, did not emphasize the 'family banking 'system in their thinking and by 1972, at a family reunion, not a single Vanderbilt was a millionaire.

Control: Investing is not about where your money is; it is about how you use it to create wealth. This is far different than buying a stock and praying it will go up. Warren Buffett never buys 100 shares of a company and just holds it. If he thinks it is a good investment, he buys enough shares to control it. By controlling it, he can create value which in turn creates wealth. The first thing wealthy families do is they gain control of their wealth. Next they invest in the family first to guarantee that wealth continues for generations forward. This gives family members a permission slip to take 'risk' they otherwise couldn't such as starting a business or investing in the stock market. Then they teach those same future generations how to continue this process. Today, in generating family wealth and saving future generations, dabbling in stocks will never provide the ownership and control that is needed. The elements that affect these types of legacies are taxes, risk, creditors and luck. In your defense, you have been following the failed traditional retirement strategies because Wall Street, the government and media pundits have convinced you this is the only way to create wealth.

Leverage: Leverage is the ability to expend the least amount of money to create the most wealth. Unfortunately, following traditional planning does not create multiples of wealth immediately. If it did, you wouldn't be worried about running out of money. If a family asset is not being used to generate income then that asset should be used to create family generational wealth. This includes time, which will be one of the most important assets a family member has. You would want to insure and guarantee that the wealth be transferred to the family income tax free.

The contract: If you were able to invest in the oldest member(s) of the family and they allowed you to do so to create the ultimate family legacy, what investment would be used? Life Insurance. Like in the alternative retirement planning idea we put forward, life insurance enables the contract owner to leverage one's contributions into a multiplied benefit ultimately paid out in an income-tax free death benefit; life insurance allows the contract owner control and use of their account or cash value which could be used for paying for college, buying a car or house and creating a defined benefit payout in retirement all income tax free. Life insurance is the perfect solution for family wealth creation, creating a ‘family banking system’ and helping to elevate the financial catastrophe our future generations face.

Ed Slott, the man known as “America’s IRA Expert” and host of numerous PBS shows on the subject of retirement, even he says “Life insurance is the greatest and most under-utilized loophole in the tax code.” It is a contract the family controls. The cash values and death benefit in a life insurance policy grow tax deferred and income-tax free. They are protected from creditors in most states and passes outside of probate. Any number of family members including parents can contribute to the premiums. This creates the greatest amount of death benefit that will pass on to the family.

This isn’t about buying insurance and hoping for someone to die. Nor is it about some insurance agent trying to make a big commission. All this is centered on the legacy of love. This is about the unfortunate position traditional retirement planning has put most Americans in today. This is about moms and dads, grandmas and grandpas, having one last opportunity to help their children and grandchildren fulfill the goals and dreams they have for them. This is about giving people hope and leaving our world just a little bit better than we found it. This will be a very emotional decision and should be viewed with the proper perspective.

Not just any adviser, broker or agent can properly structure this, though most will claim they can. My first question to the current advisors, brokers and agents you may be working with would then be, “Why didn’t you do this for me already?” You need someone with vast knowledge and experience in doing this. The design of your insurance contract needs to be carefully constructed to meet your family’s objective. This strategy won’t or can’t work for everyone but it is the one that offers the best opportunity and potential for success.

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