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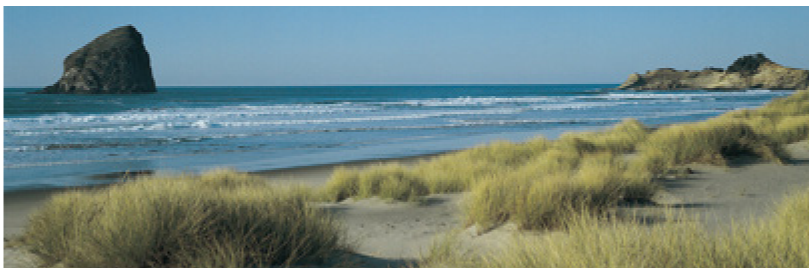

THE FINANCIAL FORMULA

Giving You The Financial Information You Need

August 2016

Hello FF readers! Please enjoy the July '16 edition of The Financial Formula (I know it says "August" but we'll send one later this month also). Please let us know if you have any questions - thanks!

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In This Issue

The DOL Revisits Conflict of Interest Rules

New regulations -- so-called "conflict of interest" rules -- impacting retirement savers and the financial professionals who serve the retirement industry were introduced by the U.S. Department of Labor (DOL) in April 2016.

Obstacles to Avoid on the Road to Investment Growth

Most long-term financial goals require you to maintain a long-term investment outlook. Don't let your goals be sidetracked by these potential obstacles.

When Should You Collect Social Security?

When should you begin collecting Social Security? The answer depends in part on how long you think you'll be around to collect it.

The DOL Revisits Conflict of Interest Rules

Over the past several decades, there has been a significant shift in the retirement savings landscape away from employer-sponsored defined benefit pension plans to defined contribution plans, such as 401(k)s. At the same time, there has been widespread growth in assets in IRAs and annuities.

One consequence of this change, according to the U.S. Department of Labor -- the governmental body that oversees pensions and other retirement accounts -- is the increased need for sound investment advice for workers and their families.

The DOL says its so-called "conflict of interest" rules are intended to require that all who provide retirement investment advice to employer-sponsored plans and IRAs abide by a "fiduciary" standard -- putting their clients' best interest before their own profit.

Originally proposed more than a year ago, the "final" rules -- introduced in April 2016 -- have been revised to reflect input from consumer advocates, industry stakeholders, and others. Following are some of the key takeaways from the DOL's final regulatory package.

According to the DOL's definition, "a person is a fiduciary if he or she receives compensation for providing advice with the understanding that it is based on a particular need of the person being advised or that it is directed to a specific plan sponsor, plan participant, or IRA owner."

The Role of the Fiduciary

According to the DOL's definition, "a person is a fiduciary if he or she receives compensation for providing advice with the understanding that it is based on a particular need of the person being advised or that it is directed to a specific plan sponsor, plan participant, or IRA owner. Such decisions can include, but are not limited to, what assets to purchase or sell and whether to roll over from an employment-based plan to an IRA. [1] In this capacity, a fiduciary could be a broker, registered investment adviser, or other type of adviser.

The Best Interest Contract Exemption

The DOL's final rules include a provision called the Best Interest Contract Exemption (BICE). This exemption is intended to allow firms to continue to use certain compensation methods provided that they "commit to putting their client's best interest first, adopt anti-conflict policies and procedures, and disclose any conflicts of interest that could affect their best judgment as a fiduciary rendering advice" -- among other conditions.[2]

How does the BICE affect you? The contract provisions of the BICE are slated to go into effect January 1, 2018. At that time, IRA clients entering into a new advisory relationship should expect to sign the contract either before or at the time that a new recommended transaction is executed. IRA clients already working with an investment adviser as of January 1, 2018, may receive a notice from their adviser describing their new rights, but they should not be required to take any action unless they object to the terms of the notice.

Clients receiving advice about investments in an employer-sponsored retirement plan should receive the same general protections and disclosure, but should not expect to receive a contract to sign.

Education vs. Advice

The DOL's final rules clarify its position that education about retirement savings is beneficial to plan sponsors, plan participants, and IRA owners. As such, the DOL said that plan sponsors and service providers can offer investment education without becoming investment advice fiduciaries.

Further, the DOL stated that communications from plans that identify specific investment alternatives can be considered "education" and not a "recommendation" because plans have a fiduciary who is responsible for making sure the investment offerings in the plan are prudent. Since there is no such responsible fiduciary in the IRA context, references to specific investment alternatives are treated as fiduciary recommendations and not merely education.

Time to Get on Board

The new regulations are expected to take effect in the spring of 2017 (at the earliest) to allow all affected parties to adapt to and incorporate the changes.

To learn more about the new regulations and how they may affect you, visit the Department of Labor website.

United States Department of Labor, "FAQs About Conflicts of Interest Rulemaking."

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Obstacles to Avoid on the Road to Investment Growth

By investing in a well-thought-out mix of investments, you'll give yourself an opportunity to take advantage of whichever asset type happens to be thriving at a particular time.

You're in the driver's seat when it comes to choosing investments for your retirement savings. Make too many wrong turns, however, and you may not achieve your long-range financial goals. Here are some common roadblocks to avoid.

The Poor-Diversification Block

You're free to choose from the range of investment options your plan offers, but concentrating too much of your retirement money in one investment type may not be wise. Some investments do much better than others -- at times no one can predict. By investing in a well-thought-out mix of investments, you'll give yourself an opportunity to take advantage of whichever asset type happens to be thriving at a particular time.

Choosing a mix of different investments (diversification) is also a proven strategy for managing investment risk.[1] When one type of investment is down, another may be up or holding steady, adding stability to the overall value of your account.

When planning your investment mix, remember the differences in growth potential of the various asset classes. For instance, the historical returns of investments such as money market funds are often close to the rate of inflation and may be too low to deliver the long-term growth you need.[2] On the other hand, if you have a heavy concentration of potentially high-earning stocks and the market performs poorly, you risk losing a lot of the value of your account, at least temporarily.[3]

The Quick-Escape Block

Expect the stock market to decline at times. It's inevitable -- only the timing is uncertain. When stock prices drop, don't automatically veer off course by moving your stock investments to bonds or another asset class that may be doing better at the time.[4] Instead, it may be prudent to "stay the course" so that you'll be in a better position to benefit from potential future growth down the road.

The Spend-the-Future Block

If you change jobs, you'll have the option of cashing out your retirement account. You may be tempted to take the money and spend it, especially if the amount isn't very large. But, if you spend your retirement money, making up for it later may be very difficult.

The chart below shows just how costly spending a retirement nest egg can be. A much better strategy: Roll over your retirement money into an individual retirement account (IRA), into your new employer's tax-deferred retirement plan, if allowed, or leave it in your current plan, if allowed. You'll likely still be able to choose how your retirement money is invested. And you'll keep it working for you until you're certainly going to need it -- after you retire.

The "Cost" of Withdrawing $25,000

	Retirement Account Balance at Age 30	Amount Withdrawn at Age 30 When Changing Jobs	Balance at Age 65
Employee A	$25,000	$0	$512,786
Employee B	$25,000	$25,000	$225,132
		Cost of Early Withdrawal	**$287,654**

Assumes: $125 monthly contributions and 7% average annual investment returns between ages 30 and age 65. Withdrawals are subject to income taxes at then-current rates and a possible 10% additional federal tax if withdrawn prior to age 59½. The chart does not reflect these costs. This is a hypothetical example. Your investment return and contributions will vary.

Source: DST Systems, Inc.

[1]*There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not assure against market risk.*

[2]*An investment in a money market fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the fund.*

[3]*Investing in stocks involves risks, including loss of principal.*

[4]*Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and are subject to availability and change in price.*

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When Should You Collect Social Security?

Those choosing to collect before their normal retirement age face a reduction in monthly payments by as much as 30%.

A growing number of Americans have been forced to delay their planned retirement date due to job and savings losses suffered during the past five years. According to a survey, 40% of U.S. workers said they have resolved to retire later due to concerns about outliving their savings and fears of rising health care costs.[1] Postponing retirement not only means working longer, but also delaying when you start collecting Social Security. Currently, workers can begin collecting Social Security as early as age 62 and as late as age 70. The longer you wait to start collecting, the higher your monthly payment will be. Your Social Security monthly payment is based on your earnings history and the age at which you begin collecting compared with your *normal retirement age*. This *normal retirement age* depends on the year you were born.

Year Born	Normal Retirement Age
1937 or earlier	65
1938	65 and 2 months
1939	65 and 4 months
1940	65 and 6 months
1941	65 and 8 months
1942	65 and 10 months
1943-1954	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 or later	67

Those choosing to collect before their *normal retirement age* face a reduction in monthly payments by as much as 30%. What's more, there is a stiff penalty for anyone who collects early and earns wages in excess of an annual earnings limit ($14,160 in 2011).

For those opting to delay collecting until after their normal retirement age, monthly payments increase by an amount that varies based on the year you were born. For each month you delay retirement past your normal retirement age, your monthly benefit will increase between 0.29% per month for someone born in 1925, to 0.67% for someone born after 1942.

Which is right for you will depend upon your financial situation as well as your anticipated life expectancy. Anyone with a good pension or substantial savings may want to delay a bit. Similarly, if you're in no hurry to retire, you may want to continue working longer and collect later.

Likewise, those with a family history of longevity who expect to live a long time stand to gain more by delaying. If you think it unlikely to survive beyond age 78, you may want to start collecting at age 62. And if you expect to survive beyond age 82, you might consider a delayed collection.

Whenever you decide to begin collecting, keep in mind that Social Security represents only 38% of the average retiree's income.[2] So you'll need to save and plan ahead -- regardless of whether you collect sooner or later.

[1]*Source: Towers Watson, October 2010.*

[2]*Source: Social Security Administration, "Fast Facts & Figures About Social Security," August 2011.*

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