

# Rewirement: Rewiring The Way You Think About Retirement

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# Speaker

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- American Bar Foundation Fellow
- American Bar Association Top 40 Young Attorney
- InvestmentNews Top 40 Under 40 Financial Services
- Trusts & Estates Distinguished Author
- Author of Rewirement

# Overview

- Power of Process
- How We Make Decisions
- Retirement Income Planning

# The Value of Process



# **Process Provides A Blueprint For Success**

# Why Process is Important

- Michael Phelps
  - 23 Gold Medals
  - 39 world records
- It was about the process!



# Understanding the 'Human' Element in Decision Making



# The Rational Paradox

Markets Are Efficient





# Or is it? The Rational Paradox

**“A person is smart, People are dumb”**

- Agent K, Men In Black

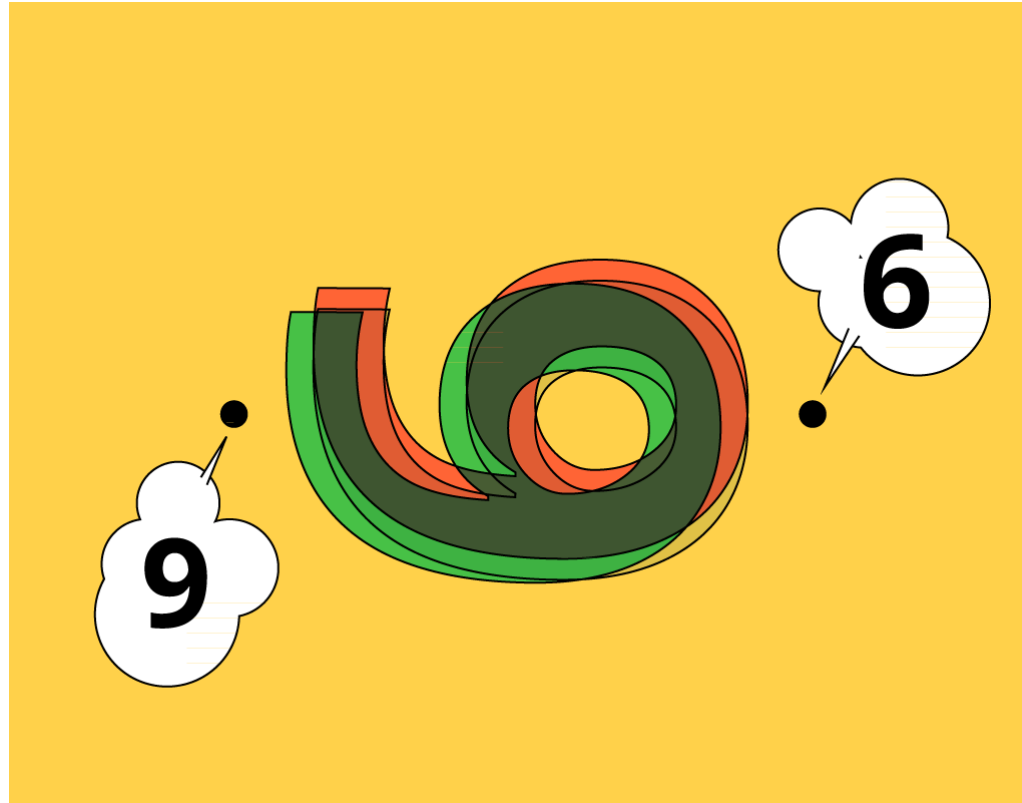


# What is rational decision making?

People need to stick to some basic elements of “consistency and coherence”

# Framing of Decisions

# Value of Perspective





# What do you see?





# What if you zoomed out?






# Narrow Framing


**Focus on the short term, can't see big picture**

Example: make investment allocation decisions without considering big picture or time horizons

# A Look At Decision Making Through The Risk Decision Frame



- 
- **Fear**  
(can drive our decisions)
  - **Uncertainty**  
(can create hesitation)
  - **Pain and Loss**  
(we tend to want to avoid)



Source: katie-moum-  
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# Loss Aversion

- Most people are more subject to loss aversion (roughly 2.5 times the pain they get from loss they get pleasure from gain)\*\*
- But, about 66% deviate from median - 20% are much more loss averse than average, 10% are gain seeking, and 1/3 treat losses and gains almost equal\*\*\*

\*\* Tversky & Kahneman, "Advances in prospect theory" 1992

\*\*\*Payne, Shu, Webb, Sagara 2016



# Loss Aversion Impacts

- Most people are loss averse
- People want the sure thing when it comes to gains
- People are willing to chase risk when it comes to avoiding loss
- Additionally, ambiguity aversion hypothesis (Ellsberg, 1961) says people prefer known probabilities over the unknown

# Getting To Know The Future You

# Thinking About The Future

- How often do you think about 5 years from now?
  - About 25% say rarely or never
- 10 years?
  - About 33% say rarely or never
- 30 years?
  - About 55% say rarely or never

<https://www.iftf.org/future-now/article-detail/survey-finds-majority-of-americans-dont-think-about-the-future/>



## Do You Care About The Future You?

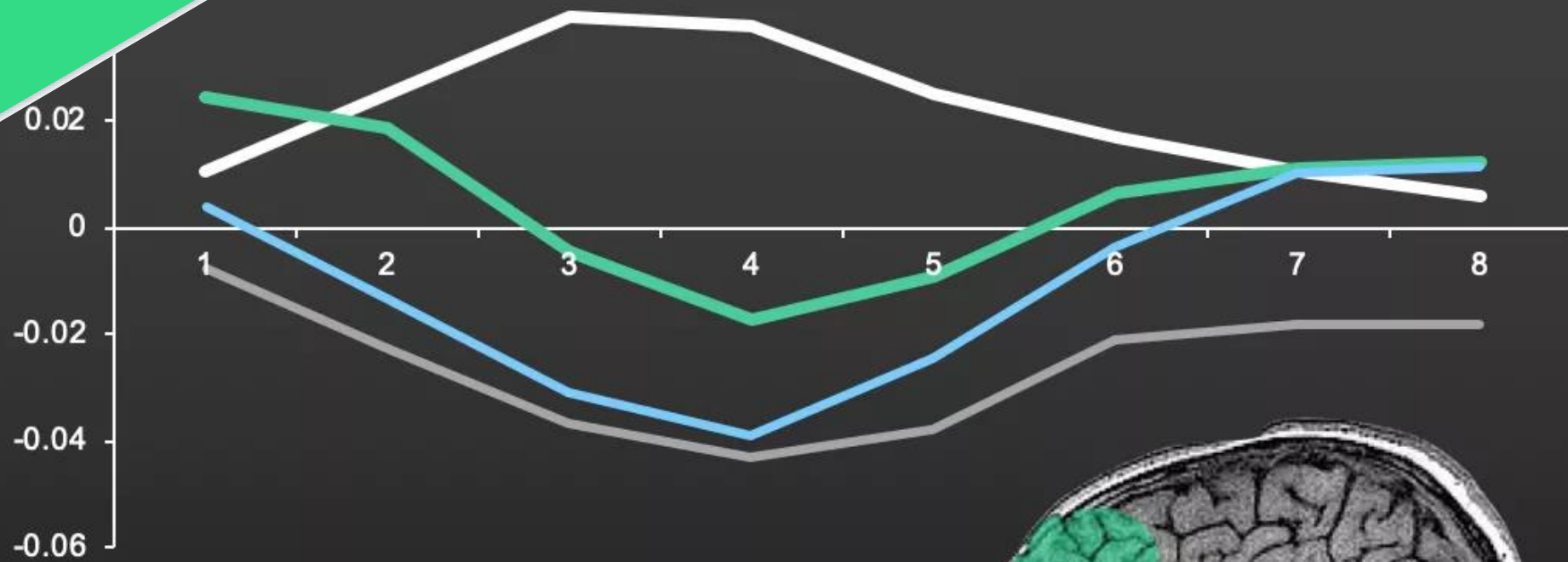
I never get enough sleep. I stay up late at night, cause I'm Night Guy. Night Guy wants to stay up late. 'What about getting up after five hours sleep?', oh that's Morning Guy's problem. That's not my problem, I'm Night Guy. I stay up as late as I want.

So you get up in the morning, you're exhausted, groggy... ooh I hate that Night Guy! See, Night Guy always screws Morning Guy. There's nothing Morning Guy can do.

The only thing Morning Guy can do is try and oversleep often enough so that Day Guy loses his job and Night Guy has no money to go out anymore.

– Jerry Seinfeld





- CURRENT SELF
- FUTURE SELF
- CURRENT OTHER
- FUTURE OTHER



# How To Make Future Self Closer

- Interact with photo of aged person – more likely to save for retirement (Hersfield, Goldstein, et al. 2011)
- Aged Selfie plus a nudge-link (increased savings) (Robalino & Hersfield - AforeMovil Paper)
- Ask Questions about what you will do in the future (Shah, Hersfield, Working Paper 2019)
- Talk about future first (Christensen, Hersfield, & Maglio)
  - How similar is 2018 you to 2048 you?
  - How similar is 2048 you to 2018 you? 5.4% more likely to invest



# Retirement Income Planning



# Behavioral Biases In Retirement

- Risk aversion over long period of time could be harmful
- Don't know how to spend down
- Spending feels like loss
- Prioritizing the now
- Superman syndrome – overstating one's own health
- Narrow focus – don't prioritize spending needs in future like long-term care





**What do people learn  
about when working  
as it comes to  
retirement planning?**



# SNS

Saving. NOT. Spending.



# Literacy Concerns

2014 & 2017 RICP Retirement Income Literacy Report showed that only roughly 25% of retirement age Americans could pass a retirement income literacy quiz!

Source: <https://www.onefpa.org/journal/Pages/JAN19-Retirement-Income-Literacy-A-Key-to-Sustainable-Retirement-Planning-.aspx>



We need to **rewire** how  
we think about **saving**  
for retirement into how  
we think about **spending**  
in retirement!



# Investing Flipped On Its Head

## Plentiful Penny Example:

1. Penny gets an average rate of return of 0%
  2. Start with \$100,000 and need \$11,000 of income each year
  3. 5 years: 40%, 20%, 0%, -20%, -40%
- \$129,000 at end of year 1
  - \$143,800 at end of year 2
  - \$132,800 at end of year 3
  - \$95,240 at end of year 4
  - \$46,140 at end of year 5



# Investing Flipped On Its Head

## Bad Luck Betty Example:

Betty gets an average rate of return of 0%

Start with \$100,000 and need \$11,000 of income each year

5 years: -40%, -20%, 0%, 20%, 40%

- \$49,000 at end of year 1
- \$28,200 at end of year 2
- \$17,200 at end of year 3
- \$ 9,640 at end of year 4
- \$ 2,490 at end of year 5
- (Penny had \$46,140)



We need to **rewire** how  
we think about **saving**  
for retirement into how  
we think about **spending**  
in retirement!



# Building A Retirement Income Plan

# Does Advice Help?

<u>Strategies</u>	<u>Increase in Income*</u>
Social Security Claiming	9.0%
Dynamic Withdrawal Strategy	8.5%
Tax Efficiency	8.2%
Total Wealth Asset Allocation	6.1%
Annuity Allocation	3.8%
Liability Relative Optimization	2.2%
<b>Total</b>	<b>38%</b>

<https://www.morningstar.com/content/dam/marketing/shared/research/foundational/677796-AlphaBetaGamma.pdf>





**Retirement income  
planning can be like  
hitting a moving target  
in the wind.**





# What is Our Goal (the Target)?

- What do we want to accomplish?
- Where do we want to live?
- What is our lifestyle?
- Charitable goals?
- Risk tolerance?
- Long-term care planning?



# Why Does the Target Move (Longevity)?

## Longevity Risk

- How long do you expect to live?
  - Uncertain
  - Social Security says roughly 84 for males and 86 for female
- Remember averages are just a starting point
  - 1 in 3 will live past age 90
  - 1 in 7 will live past 95

Source: [www.ssa.gov/planners/lifeexpectancy.html](http://www.ssa.gov/planners/lifeexpectancy.html)



# So Many Issues to Face (The Wind)

- Inflation
- Health Care
- Market Risks
- Public Policy
- Taxes
- Long-Term Care



# What is Retirement Income Planning?

## Goal-Based Planning

### Meet your financial goals

- ▶ Income needs
- ▶ Contingent expenses
- ▶ Legacy goals

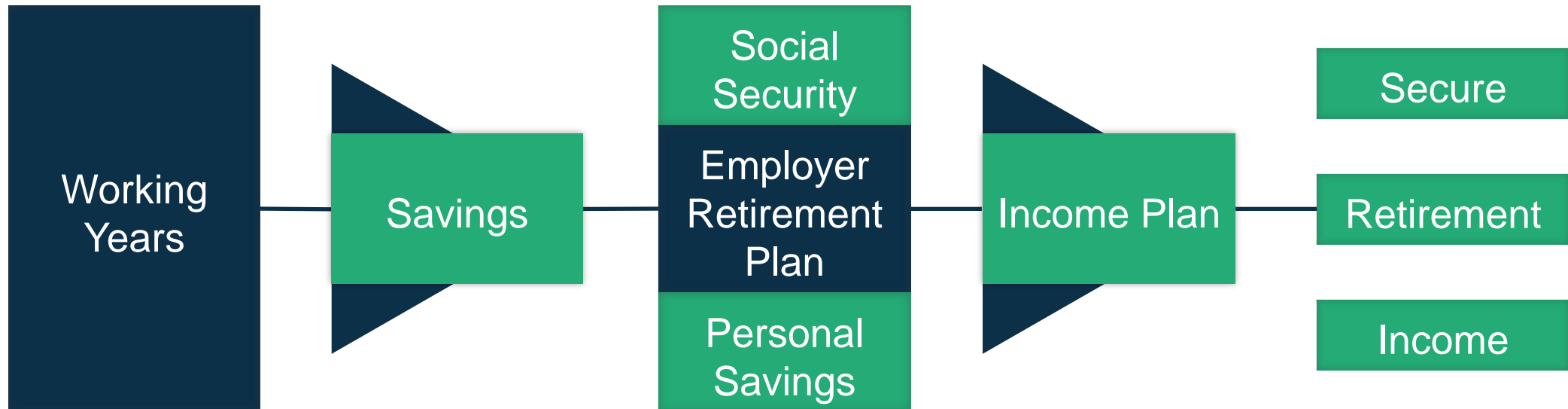



### Address retirement risks

- ▶ Longevity
- ▶ Inflation
- ▶ Healthcare
- ▶ Long-term care
- ▶ Sequence of withdrawal risk
- ▶ Public policy risk

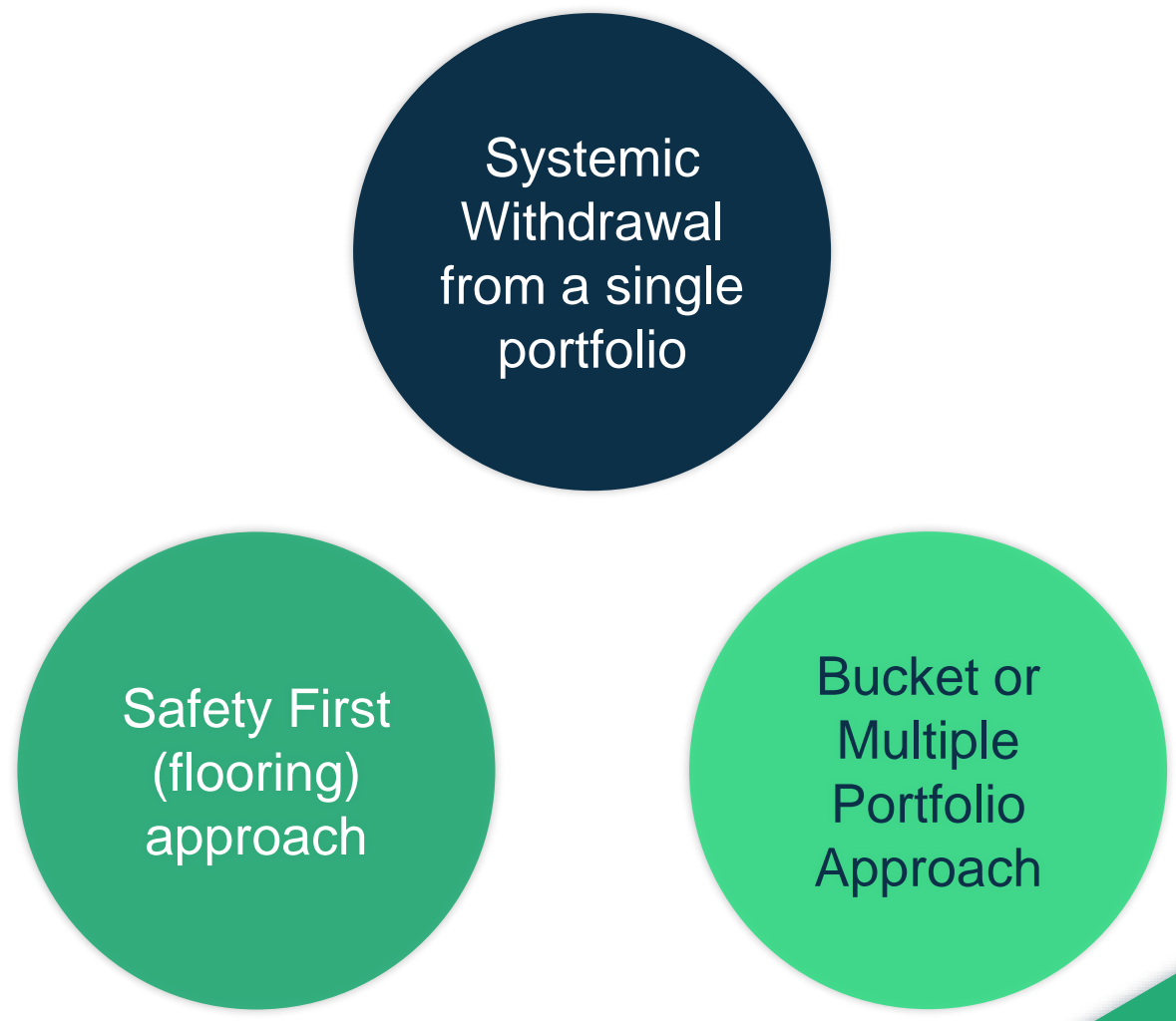
**= Secure Retirement Income Plan**

# So What is the Challenge?





# Determine Approach to Generating Retirement Income



Systemic  
Withdrawal  
from a single  
portfolio

Safety First  
(flooring)  
approach

Bucket or  
Multiple  
Portfolio  
Approach

# Flooring Strategy


Discretionary


Portfolio  
Reserves

Essential

Pensions  
Social Security  
Income Annuities



- 
- **Fear**  
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Source: katie-moum-  
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# Bucket Approach



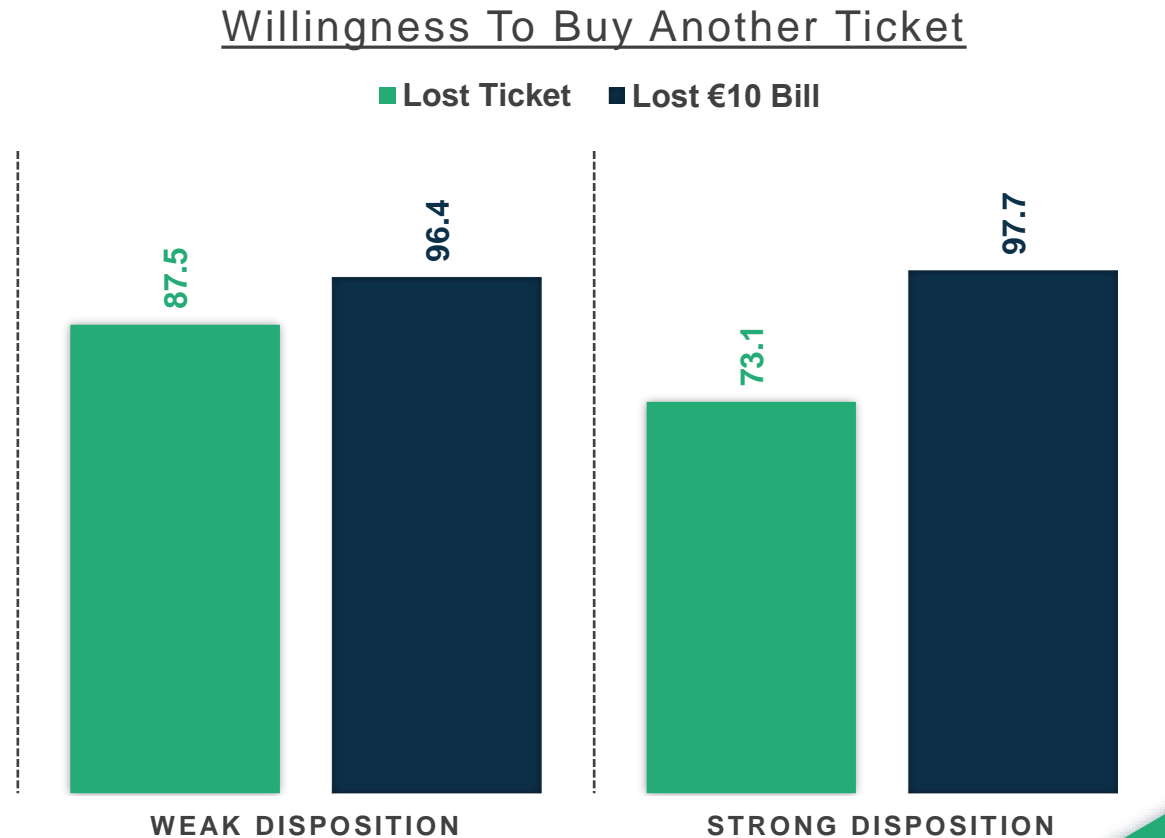


# What is Mental Accounting?

1. Money is fungible – we shouldn't care which dollar goes to what spending need
2. But, people do care – we separate funds or value in our head for different needs – i.e. **MENTAL ACCOUNTING**
3. This can create "irrational" or inconsistent outcomes

# Lost Movie Ticket Example

- Mental Accounting Scale



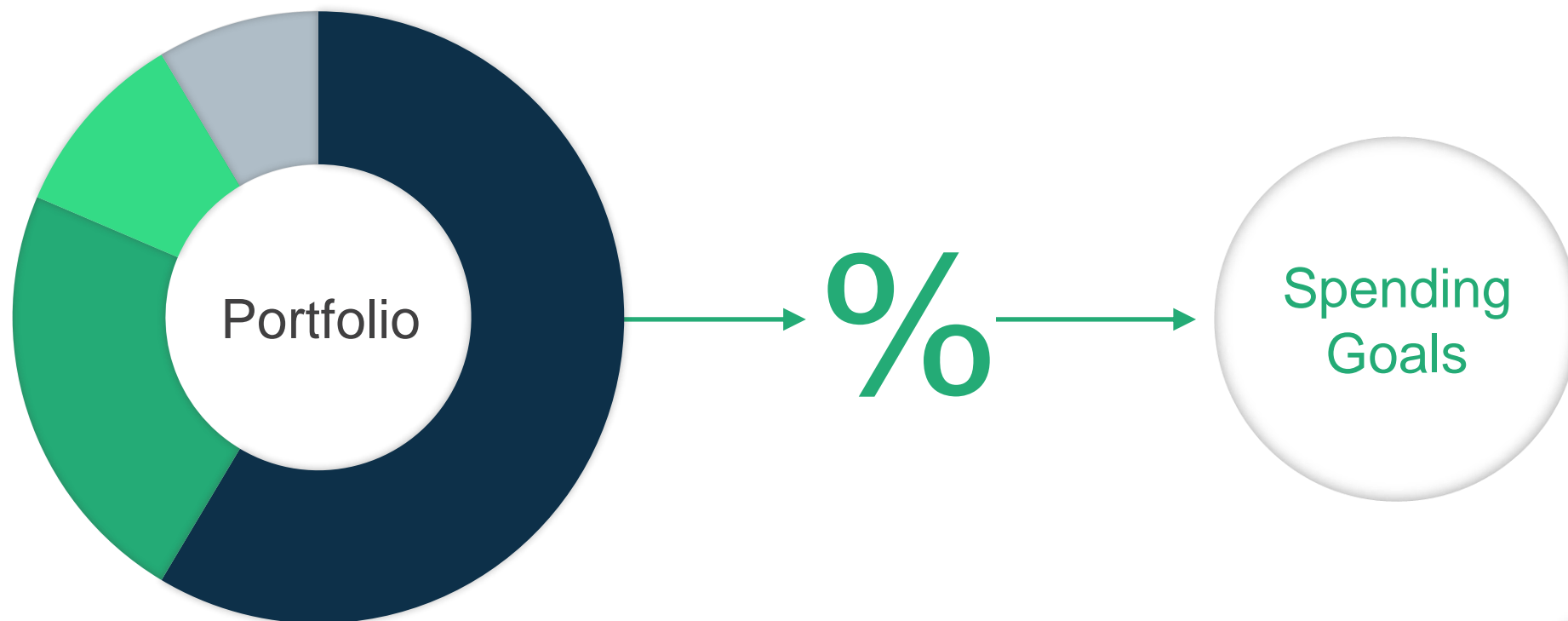


# Tax Refund v. Casino Winnings


	Experimental condition				Total (N = 114) M (SD)
	Tax refund		Casino winnings		
	€25 (n = 31) M (SD)	€250 (n = 29) M (SD)	€25 (n = 26) M (SD)	€250 (n = 28) M (SD)	
Present for oneself	3.32 (1.40)	3.48 (1.50)	3.35 (1.98)	2.93 (1.39)	3.27 (1.56)
Birthday/Christmas presents	4.23 (1.43)	3.93 (1.13)	4.19 (1.58)	4.04 (1.29)	4.10 (1.35)
Clothing	3.16 (1.19)	3.55 (1.64)	2.73 (1.25)	2.61 (1.23)	3.03 (1.37)
Eating at restaurants	3.84 (1.81)	4.41 (1.52)	3.77 (1.53)	4.43 (1.26)	4.11 (1.56)
Savings	3.81 (1.92)	3.24 (1.77)	3.42 (1.65)	3.29 (2.00)	3.45 (1.83)
Paying the bills	2.65 (2.01)	2.38 (2.01)	3.54 (1.98)	3.71 (2.24)	3.04 (2.11)
Frivolous expenses <sup>a</sup>	3.57 (0.77)	3.66 (0.80)	3.42 (0.59)	3.19 (0.58)	3.46 (0.71)
Serious expenses <sup>b</sup>	3.23 (1.22)	2.81 (1.32)	3.48 (1.09)	3.50 (1.01)	3.25 (1.19)
Spending category index <sup>c</sup>	0.34 (1.85)	0.84 (2.03)	−0.06 (1.56)	−0.31 (1.51)	0.22 (1.79)

N = 114. Ranks ranged from 1 (most likely) to 6 (least likely). <sup>a</sup>Frivolous expenses = present for oneself, birthday/Christmas presents, and clothing. <sup>b</sup>Serious expenses = savings and paying the bills. <sup>c</sup>Spending category index = mean rank of frivolous expenses – mean rank of serious expenses.

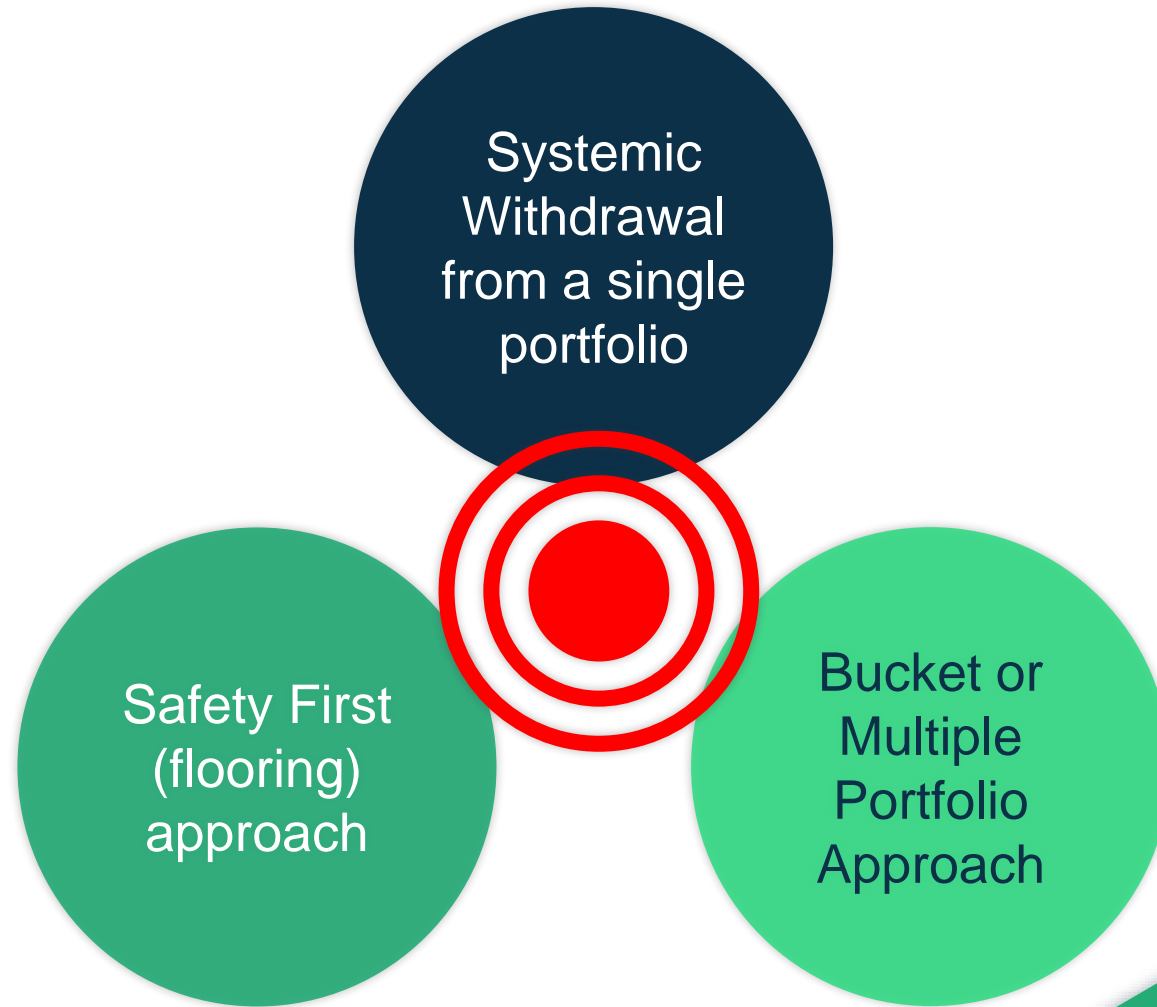
# Systematic Withdrawal



# Concluding Thoughts



# Determine Approach to Generating Retirement Income





# Retirement Income in 2022

- Have a plan in place
- Review beneficiary designations after SECURE Act
- Estate planning documents updated
- Tax Loss Harvesting
- Correct insurance
- What is coming via taxes?

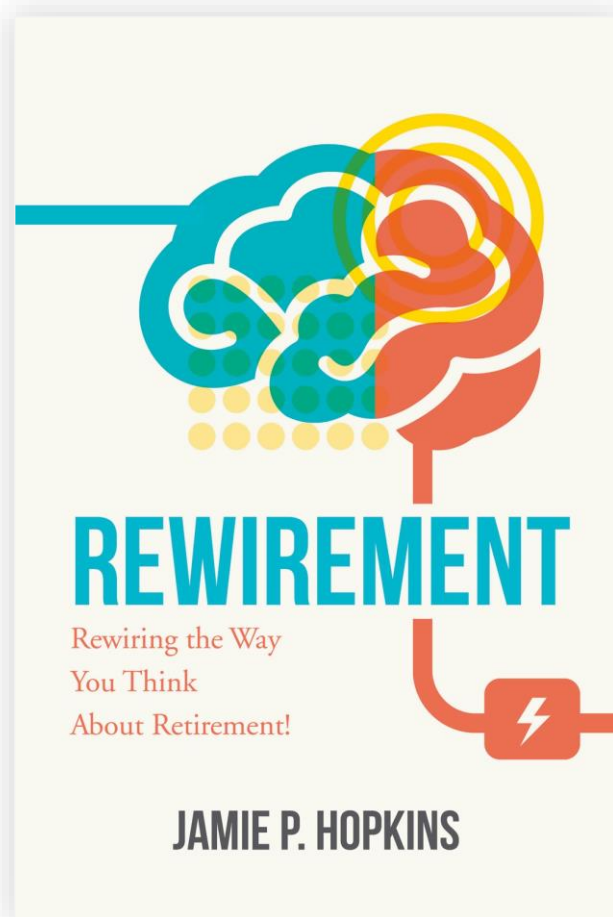


# Last Thoughts

- Take Care of Yourself so you can take care of others
- This could be a long run – with August to a full year of health issues projected (early on in view of timeline)
- Butterfly effect here is possible, economy, recession, jobs, lives, etc.
- Clarity of outcomes is not what we have now
- Take action to improve your financial situation



Questions?



# Rewirement: Rewiring The Way You think about Retirement Income

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