Retirement Daily

Saving/Investing for Retirement

The Missing Ingredient in Most Retirement Plans

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By Brad Pistole

Do you have a favorite recipe that you know so well that you don't even have to look up the recipe when you start cooking? I have a handful of meals that I love to cook and I've prepared them so many times, I never have to look at a recipe.

One of my favorite meals to make -- and probably the one that is requested the most by my family -- is chili. I've been making this chili for over 30 years.

Recently, my daughter called and asked me to make my famous chili for a weekend visit. I agreed and got to work. I prepared and put everything into the slow cooker and let it do its thing for the next few hours. Just before they arrived, I grabbed a spoon and put a small helping into a bowl so I could taste it. I immediately knew something wasn't right. So, I looked through all my ingredients, including the secret ones, and I realized what I had done.

Apparently, adding chili powder to a chili recipe is vitally important. Leaving out the smallest, seemingly insignificant ingredient in any recipe can have a huge effect on how that meal turns out. Ask any cook what happens when you forget the salt, the sugar, the yeast, or yes, the chili powder.

Life is funny like that. The smallest things can be extremely important. Did you know retirement accounts work just like recipes? There are ingredients that are vital when you're trying to prepare for the retirement of your dreams.

For almost a decade, I have been blessed to be associated with Ed Slott, who has been called "the best source for IRA advice" and America's IRA expert. Ed is a CPA and he's one of the smartest people I've ever met. Ed will often talk about the things that you should be doing to have the retirement of your dreams.

On one of his PBS television shows, he talks about what he calls the Five Silent Retirement Killers. Those five things are: taxes, risk, saving money, uncertainty, and inactivity. He realizes just how important it is for people to not gamble with their retirement funds. That's why risk is the No. 2 thing on his list of the top five retirement killers. And that's why safety should be one of the main ingredients in every retirement plan.

Over the past decade, I have met thousands of people and listened to their very personal stories of what has happened to them with their previous investment experiences. In my opinion, the No. 1 ingredient missing from almost every single portfolio I've ever reviewed is safety.

Ed will often say, "It's not what you make, it's what you keep that counts." Sure, making a 15% return is great, but when you lose 40% of your total account value during a market crash like many people did in 2001, and again in 2008, you will not be able to live the retirement of your dreams.

The numbers don't lie: If you lose 20% in an investment, you need to make 25% to get back to where you started. A 30% loss requires a 43% gain to break even, but a 50% loss requires a 100% gain just to get back to even.

For over a decade, I have been telling retirees and pre-retirees that the most important ingredient in your retirement recipe is safety. You simply do not have to take unnecessary risks to build the retirement of your dreams.

In fact, taking too much risk can absolutely destroy your retirement plan. Especially if you are taking distributions from your accounts at the same time. This is what I call the triple whammy. Once you start taking distributions from your retirement accounts, you simply must avoid losses and fees. If withdrawals, losses, and fees take place at the same time long enough, you will find yourself right back at work. That's why the missing ingredient in most of the retirement accounts I see today is safety. It is also why Will

Rogers has been attributed with saying, "I'm not as concerned about the return *on* my money as I am the return *of* my money." Simply put, safety matters.

What steps should you take if you are nearing retirement or are already retired and want to make sure you have the right plan in place? You might be asking yourself, "How much of my portfolio should I have safe vs. risking higher potential gains?"

The first thing you need to do is to take an inventory of your current investments by listing out what you are invested in.

The second piece of advice would be to decide what percentage you are comfortable leaving at risk in any type of variable or market driven account. For instance, you might be comfortable risking 50% of your portfolio for the possibility of higher gains. Another person might only be comfortable with 30% risk, while another person might not be comfortable with any risk at all.

There are only two types of accounts: those in which the principal is guaranteed and insured and those that are not.

The following types of accounts are either insured or principal protected: checking and savings accounts, certificates of deposit, money market accounts; fixed and fixed indexed annuities; many types of life insurance, like whole life insurance and cash value insurance such as indexed universal life policies. These accounts offer you principal protection and they are insured. If structured correctly, they can also offer you lifetime income that you can never outlive.

There are other types of accounts that are not principal-protected. They do, however, offer the potential for higher gains when compared to safe products and accounts. They include variable annuities and variable life insurance policies; stocks, bonds, mutual funds, and REITs (real estate investment trusts.)

Variable annuities can be particularly risky.

Just imagine this. Let's say you have $500,000 invested in a variable annuity as your main source of retirement income. You decide that you want to start withdrawing $30,000 a year to live on and in the first year, after taking your withdrawal, the market takes a 20% dip. By the time you withdraw $30,000 for income, subtract the 20% loss, and pay the 3% to 5% average fees associated with the account, you could quickly find your account balance at $350,000 and you only took out $30,000. Do you see the problem here? You must decide what level of risk you are comfortable with and plan accordingly.

If you determine beforehand the level of risk you are comfortable with in retirement is 30% and then find out that you have 80% of your accounts held in stocks, bonds and mutual funds, you will need to change your current investment structure. You would need to move more of your funds into a safe account vehicle.

How do you determine what percentage of risk is right for you? Warren Buffet has said it best: “Risk comes from not knowing what you are doing."

That's why making your list of investments and knowing specifically what they offer and what they don't offer is so important. If you are retired, you can't afford to lose your money. You don't have the time it requires to come back from making a major mistake with your investments. I can't begin to tell you how many times over the years I have had a new client tell me, "I am just now recovering from the losses I experienced in 2008 and I can't afford to go through that again."

Don't ever forget Warren Buffett's first two rules for investing. Rule No. 1 is "Never lose money." Rule No. 2 is "Don't forget rule No. 1."

So, as you put together all the ingredients necessary to come up with the retirement of your dreams, make sure safety is the key ingredient.

About the author: Brad Pistole, a Certified Financial Fiduciary, is the president and CEO of Trinity Insurance and Financial Services www.guaranteedsafemoney.com in Ozark, Mo., the host of Safe Money Radio which airs on several stations each week in Missouri and Arkansas, and author of Safe Money Matters. Brad is also a member of Ed Slott's Master Elite Advisor Group and the National Ethics Association. He is an MDRT Top of the Table Advisor.