



Retirement Strategies That Work,
When You Don't!

PathWay recently had the chance to sit down with Dan Tresemer, Managing Partner and co-founder of OnPath Financial, LLC. Mr. Tresemer is a twelve-year veteran of the financial services industry, holds a Certified Financial Planner (CFP®) designation, and is the chief strategist for OnPath Financial's Investment and Financial Planning divisions.

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PW: Thank you for taking the time to visit with us today regarding retirement planning.

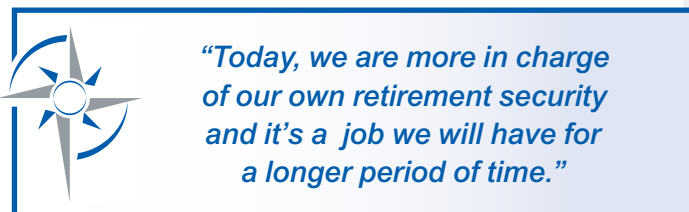
DT: I'm glad to. It is one of my favorite topics.

PW: Why is that?

DT: Because it is an issue that is "top of mind" for so many people. Today in America there is a person turning 60 years of age every 7 seconds. That trend will continue for the next two decades.¹ The "Baby Boomer" generation has transformed our world through every life stage they have encountered. Their retirement planning will be no different.

PW: If the old expression is "It's not your grandfather's Buick", then I guess "It's not going to be your grandfather's retirement".

DT: Most certainly not. There are two major factors that play into this. First of all, there was a good chance that grandpa had what is referred to as a defined-benefit pension. This is what is commonly thought of as the traditional pension, where your employer provides a fixed monthly income for life based on factors such as your pre-retirement earnings and



your years of service to the company. This type of benefit, where the company is taking care of your retirement security, peaked in the mid 1980s when there

were 175,000 plans nationwide. Back then, 75% of private sector workers had a defined-benefit plan as their primary plan. Today, there are less than 50,000 defined-benefit plans on the books.² The second phenomenon at work here is the dramatic increases we have seen in life expectancy. Over the last half century we have added almost a full decade to the average life expectancy. So today, we are more in charge of our own retirement security and it's a job we will have for a longer period of time.

PW: Why are so many employers choosing not to offer these benefits?

DT: It is important to point out that the percentage of companies offering retirement benefits to their employees has grown steadily over the last twenty years.² The migration we are seeing is away from the lifetime income benefit and towards the annual contribution to an employee's account. An example for today's worker is an employer's matching contribution to a 401(k) plan. From the employer perspective, they often times would much prefer to provide a benefit that is complete upon delivery rather than have a monthly income benefit obligation on the books for decades to come.

PW: So the average American worker is shouldering more responsibility for their retirement security.

DT: Yes. But, with more responsibility comes more opportunity. Compared to the fixed benefit programs of old, the newer, employee-directed accounts can provide greater flexibility as well as possibly provide a benefit to future generations or beloved organizations. Most traditional pension programs cease to provide benefits beyond the life of the employee and possibly their spouse.

PW: It seems that although the newer programs may be ripe with opportunity, owning your own success may be easier said than done.

DT: For many individuals, this is an area where they seek advice. If not during the accumulation phase of their retirement, then more so when they start drawing income from their accounts.

PW: Why does that transition tend to cause more people to seek professional advice?

DT: Probably because it is nothing they have done before and because the stakes are so high. When a person is saving for their retirement, they typically have two factors on their side. The first is time. If we want real growth from an investment, that means we need exposure to asset classes that can be risky and volatile, such as stocks.^a For a good portion of one's accumulation phase, time is on their side. The second factor at play is something we call dollar cost averaging. This means buying investments at periodic intervals, such as a bi-monthly contribution from your paycheck. Sometimes that purchase catches a market low and things go up from there. Sometimes the exact opposite occurs. Either way, periodic purchases level out the ups and downs and can help make an account less susceptible to market timing. Approaching and into retirement, the natural time effect is no longer and new money contributions have ceased. Every last dollar has been saved, and now we need income from those dollars for 20 to 30 years...while keeping up with inflation. Most people want to make sure they get this part right!

PW: So it appears that the same investment philosophy that got you to retirement may not be appropriate while in retirement.

DT: In my opinion, that is as true a statement as you could make about retirement planning. However, I find myself all too often reading books on retirement planning that really don't propose changing the course. I refer to it as the "glide plane" approach; the thought that the same portfolio strategy that got you to retirement will suffice while in retirement.

PW: What in particular troubles you about that approach?

DT: That particular strategy focuses on maintaining a diversified portfolio of stocks and bonds, typically 60 percent stock / 40 percent bonds, and then having an annual withdrawal rate, typically 5 percent, that becomes your income every year.^b When they run the strategy through actual historical market cycles, they will tell you that 80 percent of the time you will never run out of money. However, 20 percent of the time you ended up broke.³ This predominately happens when the strategy encounters negative returns

early in retirement. For example, if in year one the 60/40 portfolio is down 10% and we are taking an additional 5% as a distribution, we start year two approximately 15% lower than the prior year. The portfolio gets off on the wrong foot and recovery can be nearly impossible. The strategy forsakes the number one rule in stock investing; making sure you have the time necessary to withstand near-term volatility. Here in early 2009, we are living through a perfect example of times when this strategy can get into serious trouble. In 2008, the Dow Jones Moderate U.S. Portfolio Index, which allocates 60% of the weighting to stocks and the rest to bonds and cash, returned negative 22.6%.⁴

PW: So how does your approach differ?

DT: At OnPath Financial, one approach we take is to attempt to create the time necessary to be a long-term investor. We know that we need some stock market exposure to beat inflation over time, but our approach employs a more segmented strategy. One track for near-term income needs and one track for long-term growth. Our work in this area has been honed through our relationship with Paul Grangaard. A CPA by trade, Paul has devoted a good portion of his career to developing this two track strategy.

PW: What types of assets make up the two tracks?

DT: It varies depending on the market environment and your personal situation, but the strategy looks like this. First, what we refer to as the income track is designed to replace your paycheck in a manner that is highly predictable. In a perfect environment, we are paving this path with enough assets to provide steady income for between 7 and 10 years. The investments in this category are boring by design. Maybe 80 percent fixed income assets and 20 percent conservative equity strategies. Our goal here is



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to not sweat where our income is coming from in the near-term while creating the time necessary for the second track of the strategy...investing for growth.

The overall strategy looks to spend down the income track over the initial time period, but as investment advisors we have created the time necessary on the growth track to pick our spots and re-pave the income track for the next 7 to 10 year period. And so on through retirement. Market corrections don't leave us scrambling, but rather allow us to stay the course knowing time is on our side.

PW: Are there any other strategies out there that have gotten your attention through the years?

DT: Believe it or not, I think the annuity industry is finally getting their act together and focusing on the right things, specifically the current generation of variable annuity contracts.^c

PW: For our readers who are unfamiliar with variable annuities, can you give them a short definition?

DT: A standard definition of a variable annuity is a long-term investment designed for retirement purposes, carrying both insurance and investment components as well as fees and charges such as mortality and expense and surrender charges for early withdrawal.

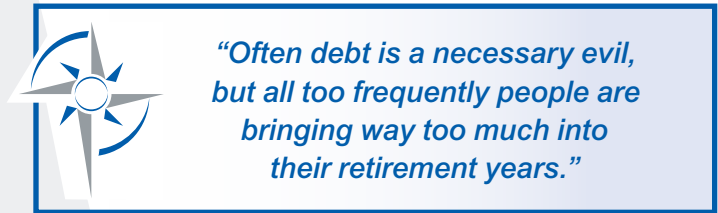
PW: Many individuals have been very critical of the use of annuities through the years.

DT: There is no doubt about that, and much of the criticism was deserved. I was very much in the “annuity skeptic” camp for much of my career. However, over the last decade or so the industry has started to develop products that are focused more on the investor. Before much of the benefits or add-ons were focused on providing beneficiaries with added benefits. A fancy death benefit is only of value if there is any money left at the end of the day. Today, the focus is on the retiree who needs income in a protected environment. Collectively we refer to this new wave of features as living benefits.

PW: Can you give us an example of how these annuity living benefits work?

DT: They come in all varieties, but the basic premise is that the annuity company will allow you to remain invested in a diversified portfolio of asset classes

while protecting your ability to withdraw a stream of income from the account, regardless of market performance.^d This is very similar to the “glide plane” approach I spoke of earlier. However, through various hedging strategies and the cost they charge for the protection feature, the company is able to



protect your ability to continue income even if you find yourself on the wrong end of the market cycle. For example, if one puts \$100,000 into one of these products, the company may guarantee your ability to withdraw \$5,000 (5%) from your account no matter what happens in the market. If the market turns south and your account goes to zero, the income will still continue throughout your lifetime. Please note, withdrawals are subject to ordinary income taxation and if made prior to age 59, may be subject to an additional 10% tax penalty. Furthermore, most companies offer a protected growth benefit which locks in the income amount if the investment achieves growth above the initial amount invested. If in year two the account has grown to \$110,000, then your protected lifetime income is based on a percentage of that higher number...\$5,500 in this example. It takes a good amount of due diligence, but there are companies that provide protection features that are worth every cent of the associated cost. They allow the client to remain fully invested while at the same time protecting the ability to generate income from this same investment. One more important note, an investor should always evaluate an insurance company's strength carefully with regard to guaranteed products and options, as guarantees are subject to the claims paying ability of the insurance company.

PW: How do you decide which strategy to employ?

DT: Every situation is unique. Remember there are always a variety of other factors at work as well. Sometimes we manage risk through creating time, such as in the first strategy I laid out. Sometimes we choose to transfer the risk by placing a portion of the client's portfolio in an annuity with income protection.

Sometimes it is a combination of the two. Our goal with our clients is to take away the worry. Many individuals have worked hard to get to the point where they can confidently retire. A good plan and a well executed strategy can ease their mind as they enter this new chapter of their lives.

PW: We have talked a lot about investing. Are there other areas within retirement planning that peek your interest?

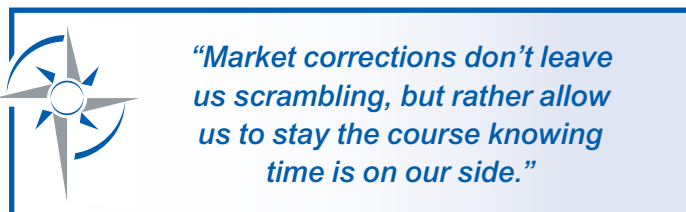
DT: Yes, a passion for helping clients avoid three common mistakes I see all too often. The first is starting to plan way too late. The second is carrying too much debt into retirement. And the third is controlling the risk of unplanned healthcare expenses.

PW: Let's take them one at a time. When is it appropriate to start planning for retirement?

DT: Now (pause). All kidding aside, the earlier you start chances are the better off you will be. You don't need to get fancy early on, but you should be doing some modeling to see if what you are doing will get you close to the retirement you envision. Once you are 10 years away from your retirement date, I feel you need to start fine tuning the plan. With our clients within that 10 year window, we know exactly where we are getting dollar one of income. If we have planned correctly, a market correction late in retirement shouldn't push back your retirement date.

PW: Talk about the debt levels you see with today's retirees.

DT: Often debt is a necessary evil, but all too frequently people are bringing way too much into their retirement years. It seems that gone are the days of buying a home and remaining there until it was paid off. Nowadays we tend to move multiple times, oftentimes using a thirty-year mortgage to buy that next home. A successful retirement can be achieved by



being a good saver, but you can also come at it from the other direction. If we can lower liabilities during our working years, then you will need less money

during retirement. A good plan will help you look at retirement planning from both directions.

PW: And finally, healthcare costs.

DT: Here I'm not talking about doctors visits and hospital stays. Your health insurance or Medicare will help with that. I'm talking about needing assistance in the home or even in a facility such as an assisted living community. It is not fun to think about, but the fact that we are living longer has increased our chances of requiring some assistance at some point during our life. The fix is easy, purchase long-term care insurance coverage. From a planning point of view, very few individuals can comfortably generate an extra \$75,000 per year from their portfolios without putting their long-term viability in jeopardy. This is a case where you simply want to transfer the risk to the insurance company...plain and simple.

PW: Thank you for your time today and your insight into this area of planning.

DT: My pleasure.

REFERENCES:

¹ Statement of Josefina Carbonell, Assistant Secretary for Aging, U.S. Department of Health and Human Services, before the Special Committee on Aging, United States Senate, February 15, 2007.

² Employee Benefit Research Institute tabulations based on U.S. Department of Labor, Employee Benefits Security Administration, Private Pension Bulletin Historical Tables (February 2008).

³ Guidelines for Withdrawal Rates and Portfolio Safety During Retirement, John J. Spitzer, Ph.D.; Jeffery C. Strieter, Ph.D.; and Sandeep Singh, Ph.D., CFA; FPA Journal, October 2007.

⁴ The Dow Jones Relative Risk Indexes measure the performance of conservative, moderate and aggressive portfolios based on incremental levels of potential risk. The indexes are designed to systematically measure various levels of risk relative to the risk of a U.S. all-stock index. Investors can identify an appropriate benchmark as the index that has the most similar historic risk characteristics. www.djindexes.com

^a Such a plan involves continuous investment in securities regardless of fluctuation in price levels of such securities. An investor should consider their ability to continue purchasing through periods of low price levels. Such a plan does not assure a profit and does not protect against loss in declining markets.

^b There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not ensure against market risk.

^c You should consider the investment objectives, risks, and charges and expenses of the variable annuity and underlying investment options carefully before investing. Prospectuses containing this and other important information about the variable annuity and underlying investment options are available upon request. Read carefully before investing.

^d Riders are additional guarantee options that are available to an annuity or life insurance contract holder. While some riders are part of an existing contract, many others may carry additional fees, charges and restrictions, and the policyholder should review their contract carefully before purchasing. Guarantees are based on the claims paying ability of the issuing insurance company.

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