<u>Why Your 401k Sucks and What to do About it.</u>

By: Chris Lynes, June 2012

Before I go into what to do about it, let's discuss the reasons why your 401k sucks, and there are several. The first is that the basic premise of the 401k is no longer valid. What was the original premise, you ask? In the 1970, and 80s, the highest tax rates were well over 50%, so when you contributed to your 401k, you deferred paying taxes until you retired many years later and, because you were retired, the tax rate would be much lower. Sounds pretty good, right? But the reality today is that, with the tax rates at historic lows, you have to ask what you taxes will be in future years relative to today. Do you think taxes will go up in the future, or down? If they go down, your tax rate at retirement will be lower and you will have won the battle of the taxes,

But, if you think taxes will go down, you have been living in a vacuum somewhere and not being aware of the constant press by our government to raise tax rates. And, if as expected, the tax rate rises, you will have been better off by putting you 401k money somewhere else. On feature of the 401k is that your employer can also contribute to you fund at a tax deferred way as well. OK, but he can also contribute to any plan you have, not just the 401k, and he can do so without limit, unlike the 401k which has many IRS restrictions attached.

One of the dirty little secrets of 401ks had been that the administrators and fund managers have not had to disclose all of the fees that come out of your fund, that is, until now. As of July 1, 2012, all parties that get any fee from a 401k must be disclosed. Fees can be 1.5% to 4% of the fund each year, and it comes out whether your fund is winning or losing. The financial industry fought against that disclosure with all they had, but, in the end, they lost.

What the new rules also added was a much increased liability to anyone who offers advice as the what investment options in the 401k to invest in. That includes anyone at the employer, third-party admin, CPAQ, and HR department employees. The penalties are large and will be highly scrutinized. Most company managers are not fully aware of this new rule, and they ignore it at their peril.

The other little known fact, reported by Forbes Magazine, is that, with the fees and market moves, an average 401k has only grown by 2.7% over the last 25 years. Is that OK with you? Experts have long determined that the 401k program is just not enough of a retirement plan. The vast majority are just not generating enough money to retire and will run out in just a few years. Is that OK with you? I'm guessing not.

The 401k program is known as a "defined contribution" program where the employer and employee ea. "contribute" a specified amount each year toward retirement. This plan has largely replaced the "defined benefit" plan that provided a defined benefit at retirement for the life of the employee. During the late 70s and into the 80s, employers embraced the 401k and you might ask why? It all very simple, it cost the employer much less and added to the company's profits. By contributing a. year, the company did not have to carry the liability of future retirement benefits. Financial institutions embraced and promoted the 401k because they now had another service they could charge fees to advise their clients for. There were some really bad issues with the 401k, but "experts", either didn't understand them, or just didn't care, but we have been sold a "bill of goods" and we are still stuck with it today. It is, however, expected that the 401k, as a retirement vehicle, will pretty much go away, or morph into something else, in the next decade.

So, what happens now , and for the future, to create retirement funds? One solution being put forward is to offer annuities within the 401k which has no annual fees other than the 401k fees.. But, I say: why would you want to put an annuity in a 401k when you can just offer the annuity directly. If that is done, then the annuity has no more IRS boundaries and regulations and the 401k administrator is no longer required so their fees would no longer have to be paid.. That's because the annuities are funded with after-tax dollars and are automatically tax-deferred until the money is extracted. Imagine, a savings plan that is not, in any way, controlled by the government. How would that work?

Instead of offering, an employer would set up a retirement annuity in the employees name. Then both the employee, and the employer, can contribute to that annuity in any amounts. 401k contributions are limited by the IRS to $17,000 annually. There are no limits to what is done with after-tax dollars because the IRS already has the taxes. This allows the employees to put whatever they like into their annuity. It also allows the employer unlimited contributions to reward employees for their service. Please note that the gains in annuities will be taxed upon extraction. This does, however, simplify retirement funds, and keep the government out of retirement planning. By eliminating the 2-4% fees in a 401k, these funds will grow larger and faster. Another feature of this planning, is that you can take out some of the money from the cash-value of the annuity for emergencies, such as medical or debt issues without penalties. Another key feature is that, if the employee leaves, he just takes the annuity with him without any paperwork issues at all. The employer just ceases to contribute. The new employer can just begin to contribute to the same annuity without paperwork issues as well. Certainly sounds better, right? This plan is good for employees up to about 60 years old, maybe even older as the retirement age increases. This is because it takes a minimum of 10 years to make an annuity pay off correctly. But, for those below 50 years old, there is even a better planning program.

Actually, this is, in my opinion, the single best savings program in existence today. This program is the IUL Policy. Yes, it is the Indexed Universal Life Policy, which is a type of like insurance policy that provides protection in case of death, serious disease, need for long-term-care, and a tax-free retirement savings program. Yes, a tax-free growth plan that is unique. The premiums are after-tax dollars, but all of the benefits of the program are all tax-free. Would you rather pay taxes on the seeds or the harvest? OK, let’s discuss this plan and how it works for you.