Pre-Retiree Wealth Building #2 – Whole Life Version

Think of this presentation as a story in chapter format. Chapter 1 is defining the purpose, Chapter 2 is defining the problem, Chapter 3 is defining solutions, and Chapter 4 is Implementation leading into the Cornerstones Calculator. You're going to help the client understand the wealth building concepts that are being discussed, and then show them how you can apply their own numbers to these concepts with the Cornerstones Calculator. All of these chapters are important to do in order. You don't want to go from one chapter to the next without making sure the concepts discussed in the current chapter are understood. This especially applies to Chapter 2. It is imperative someone recognizes the problem before going onto the solution. There are key phrases and transitions that are very important to utilize when giving the presentation. These key phrases and transitions are underlined and bold in the following script. You'll also see some italicized text/notes in areas of the script that explain the philosophy behind what the script is saying.

Chapter 1: Defining the Purpose

SLIDE 01
Title Slide.

SLIDE 02
Wealth building begins with annual savings. After that, the question is "how do we allocate our annual savings efficiently to hopefully get maximum results?" Economically, three areas are defined for allocation. One is for short term wealth building and the other two are for long term wealth building.

SLIDE 03
The short term wealth building are liquid assets, things like checking accounts, savings accounts, money markets and so forth for your emergencies, opportunities, security, and just overall peace of mind. **The question then is how do we economically define what these two long term areas are for wealth building? And the only way we would be able to answer that question is if we asked this question.**

SLIDE 04
What is the underlying premise for all long term savings anybody does?

SLIDE 05
Why are we giving up current enjoyment of our income?

SLIDE 06

The answer is to have an income stream in retirement.

SLIDE 07

It only makes sense then to understand how retirement income streams work so that we can direct the savings we are doing today in ways that potentially gives us the highest income when we retire.

SLIDE 08

In other words, how retirement income streams work economically define how to allocate our savings today. The sooner we get on an efficient path, the greater impact we have on the results.

SLIDE 09

Think about it like climbing a mountain. Is the objective to get to the top of the mountain?

SLIDE 10

Or is it really getting to the top of the mountain, and then making it back down safely? This is similar to our financial lives. Getting up the mountain is our pre-retirement/accumulation phase and getting back down is our retirement/distribution phase.

SLIDE 11

The key is that this is one continuous journey. There are two rates that make up everyone's retirement income stream later on and both are equally important. Their accumulation rate: getting up the mountain and the other is the distribution rate, getting back down safely. Knowing how retirement income streams work and then how distribution rates work, is the basis for understanding how to save money in pre- retirement.

SLIDE 12

In other words, understanding how retirement incomes streams work defines how to pack your bag in Pre-Retirement. If we don't have an understanding of how retirement incomes streams work in pre-retirement, we have no rhyme or reason as to how to allocate our savings today.

SLIDE 13

If you were going to climb a mountain would you get a guide? What if the guide said to you that they were pretty sure they can get you to the top of the mountain but they weren't sure how you were going to get back down? Would you use that guide or find a different one?

We're going to go through a short exercise and transport you to the top of the mountain. You're a retiree entering retirement. **There are typically two questions that go through people's minds at this point: 1) How much money do I need to live on? 2) How much can I withdraw without running out of money? So everyone starts to do some mental gymnastics at this point to try to justify the amount of income they want to pull from their assets as being sustainable. Many people's first mental stop for this is what we'll call a constant rate of return theory, which we'll discuss further momentarily.**

At the top of the mountain, it is critical to observe some rule changes that exist. In pre-retirement we were putting money into our assets and in retirement we are now pulling money out of our assets, so we're changing the dynamics of our money one-hundred eighty degrees. This causes a problem which is…

Chapter 2: Defining the Problem

SLIDE 14

How retirement assets react to fluctuating interest rates when money is being withdrawn for income. Let's look at an example of this.

SLIDE 15

What we have here is a person entering retirement with a million dollars, wanting to pull one hundred thousand dollars per year of retirement income to live on, which is ten percent of the initial value. The way they might justify being able to do this is by thinking they could earn a return on average, equal to or greater than, the ten percent they are pulling out which in this case is fourteen point eight four percent. And if they earn this fourteen point eight four percent constantly every single year, you can see their account grows even as they pull income out, to the point where it is close to fifteen million dollars thirty years into retirement. But, are we going to be able to earn that average yield constantly, every single year or are we going to get all of the ups and downs along the way? We're going to get all of the ups and downs. So, where does this 14.84% come from?

SLIDE 16

It comes from the history of the market, and in this case the history of S & P five hundred from 1970 through 1999. So we see each year, all the annual positive and negative yields during that thirty year period. We add them all up and divide by thirty and we get the average yield of fourteen point eight four percent. So what we are going to do now is take the fluctuating positive and negative annual yields we see here and put them into the same table we were just looking at, paying attention to what happens to our account value as we do this.

SLIDE 17

When we put the annual fluctuating returns into our table, we still have the same average yield over thirty years. But now instead of having close to fifteen million dollars at the end of thirty years, we are down to zero dollars between years thirteen and fourteen. "Why does this happen,"? It's because of the rule change at the top of the mountain, which states that any year you earn less than you pulled out, you just killed off the dollars that are supposed to be earning the returns for you. For example, a great return year is this thirty-seven percent in year six, but the issue is that you're not earning this on that million dollars you started with, you're earning that on the account value at that time, which is substantially less. **So if we are at the top of the mountain trying to use fluctuating return assets to provide us retirement income, how would we go about determining what a safe withdrawal rate might be if we can't really use a constant rate of return theory; because I've only shown you one thirty year time frame here and if I were in your shoes I'd be saying, "okay I get it, but how do I know you didn't pick the one thirty year time frame that works this way to stack the deck in your favor?",**

and I would say you're right. What you'd have to do is run thousands of simulations throughout history to determine probabilities of not running out of money at various withdrawal rates.

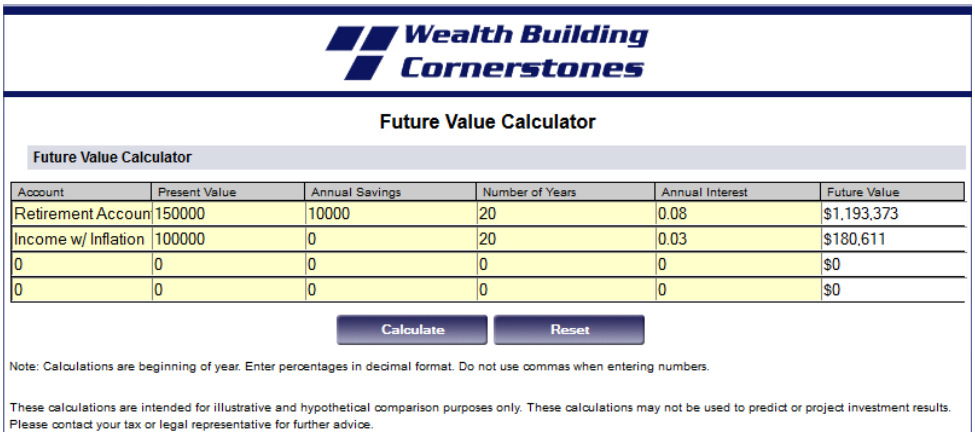
SLIDE 18 *(Ask client(s) to read this slide.)*
The industry has attempted to solve this problem for us to give us some sort of a scientific look at what is possible and they do this through Withdrawal Rate Simulations. Withdrawal Rate Simulations are software programs that use rates of returns for all types of vehicles over the last hundred years to calculate the historic probabilities of running out of money years into retirement based on the withdrawal rate chosen off the beginning asset value. These programs run thousands of simulations for every fifteen, twenty, twenty-five, thirty, and thirty-five year rolling time periods taking into account all types of market conditions and interest rate environments. The results of these simulations are the same no matter who runs them since they are using similar probability software programs and the same past market interest rate data. They are non-guaranteed.

SLIDE 19
Let's take a look at the results of these simulations. This chart shows the historic probabilities of not running out of money years into retirement based on the withdrawal rate we chose off the beginning asset base. **It is important to understand that these are withdrawal rates and not interest rates on your money in retirement. These simulations and curves exist because we are acknowledging that we have to establish our income withdrawal rate before knowing the fluctuating interest rates we will earn on our money.** As an example, let's say you chose an eight percent withdrawal rate. This would put us on the orange line on the bottom. What this is saying is thirty years into retirement, historically I've had about a five percent chance of not running out of money and around a ninety-five percent chance of running out of money. So it doesn't take a rocket scientist to tell us that by lowering our withdrawal rate we'll have a better chance of not running out of money. The financial industry has settled on a three to a four percent withdrawal rate as being a quote "safe withdrawal rate." But even at a four percent withdrawal rate, you still have around a fifteen percent chance of running out of money historically thirty years down the road in retirement.

SLIDE 20 *(Use this slide at your discretion and as needed; this slide can be helpful when someone says they would be more "conservative" as a solution to the previous slide.)*
The other component you can adjust when you run these simulations is the mixture of invested bonds. The fifty/fifty stock bond split is what we were looking at in the previous chart, and is generally one of the best performing throughout history. The bottom line is that the industry has basically settled on a three to four percent withdrawal rate off of invested assets being a quote "safe withdrawal rate."

SLIDE 21 *(Take your time on this slide. This slide is perhaps one of the most important, if not the most import slide of Chapter 2 for client interaction. It is imperative to have the client internalize what the default path means for them and the problem on this path before going onto Chapter 3.)*
As we said before, withdrawal rate simulations are really an attempted solution for pulling income from your investments in retirement. Why is it an attempted solution? **Withdrawal rate simulations might solve the issue of running out of money, but they create another issue being that a three to four**

<u>percent retirement income rate is often not a feasible solution as it will be very difficult to build the amount of assets necessary to have an adequate income stream in retirement. Because you'd need $1,000,000 to get $30-40,000/yr of retirement income. Think about it, to create $100,000/yr of retirement income you'd have to have $3,000,000-$4,000,000 in your retirement accounts. HOW FEASIBLE DOES THIS DEFAULT PATH SOUND FOR YOU? (Pause here and get response from client) See, the problem isn't really what's attainable for asset amounts, it's the withdrawal rate we set ourselves up for.</u> *(show a future value calculator example with numbers close to their own if needed here at your discretion to further cement the issue of the default path. See example below showing a calculation for the future value of their retirement account and what their inflation-adjusted income needs to be in the future, the problem is that 3-4% of $1,193,373 isn't $180,611.)*


Wealth Building Cornerstones

Future Value Calculator

Future Value Calculator

Account	Present Value	Annual Savings	Number of Years	Annual Interest	Future Value
Retirement Accoun	150000	10000	20	0.08	$1,193,373
Income w/ Inflation	100000	0	20	0.03	$180,611
0	0	0	0	0	$0
0	0	0	0	0	$0

Calculate Reset

Note: Calculations are beginning of year. Enter percentages in decimal format. Do not use commas when entering numbers.

These calculations are intended for illustrative and hypothetical comparison purposes only. These calculations may not be used to predict or project investment results. Please contact your tax or legal representative for further advice.

SLIDE 22

Bottom line is that seven to thirteen percent income rates will most likely be needed to achieve adequate income in retirement based on what's generally attainable for asset amounts.

SLIDE 23

The question is how do you do that without high probabilities of running out of money?

SLIDE 24 *(This whole presentation, Chapters 1-4, is designed to be done in one meeting, however, this is a good slide to stop at if you would like to split this presentation into two meetings. You've defined the problem and given them hope for solutions. If you do split this presentation into two meetings be sure to review Chapter 2 with them at the beginning of the next meeting before going into Chapter 3.)*
Because if I'm on these curves, trying to pull seven to thirteen percent, my chances of making it without running out of money do not look good.

<u>Chapter 3: Defining Solutions</u>

SLIDE 25

The Two Economic Powers™ Approach can enable us to do this. See, the first economic power we all have to work with is the Interest Rates/Rates of Return power which can be a good accumulator of money.

SLIDE 26

The second economic power is Actuarial Science which can be a good distribution power. These powers were always meant to work together in proper balance.

SLIDE 27

Many people used to get both powers incorporated into their long term wealth building for Retirement Income by default through Defined Benefit Pension Plans. As Defined Contribution Plans (401k, 403b, etc.) became more popular, fewer and fewer people have Defined Benefit Pension Plans.

SLIDE 28

Who bears the risk of Accumulation and Distribution for an employee's retirement income under a Defined Benefit plan? The employer or employee?

SLIDE 29

The employer.

SLIDE 30

Who bears the risk of Accumulation and Distribution for an employee's retirement income under a Defined Contribution plan? The employer or employee?

SLIDE 31

The employee.

SLIDE 32

There is a major transfer of risk/responsibility from the employer to the employee when you have a Defined Contribution Plan versus a Defined Benefit Plan. Very little education has been given to individuals regarding what they must now do to provide for themselves.

SLIDE 33

Equally important is that not only was there a transfer of risk/responsibility that occurred, but in a Defined Contribution Plan the employee is no longer getting both economic powers by default… they are getting the Interest Rates/Rates of Return power, but they must now seek out and understand how to incorporate the Actuarial Science power as they are not getting it by default.

SLIDE 34

These powers were meant to work together in balance and coordination to achieve efficient results.

SLIDE 35

When we reach retirement there are 2 global options for generating retirement income streams from the assets we've built:

SLIDE 36
1. Exchange/Trade your money. Basically in this option you would be taking money you have at retirement time and exchanging it with a financial company for a guaranteed retirement income stream.

SLIDE 37
2. If we choose not to exchange/trade our money at retirement time then the other global option is to invest our money to try to generate retirement income.

SLIDE 38
If we don't incorporate Actuarial Science we can be relegating/defaulting ourselves to the 3-4% income rate problem. When we incorporate Actuarial Science along the way we put ourselves on a path that can potentially provide higher retirement income rates from the assets we've built. The balancing between these economic powers (Cornerstones) is the key… Having too much of either can make you less efficient.

SLIDE 39
When you balance the economic powers (Cornerstones) along the way you get both retirement income options: 1) Exchanging/Trading (Covered Assets) or 2) Investing (Volatility Buffer) to choose from or combine together at retirement time to potentially provide higher overall retirement income. So how do we do this?

SLIDE 40
One of these areas that we are defining for long term wealth building is retirement assets. Things like your 401k's, growth securities, real estate and so on. Retirement assets by themselves have a big issue getting down the mountain because these assets generally use one power of the financial industry being interest rates, or rates of return. Think of this power as the accumulation power, but this power by itself puts you back on the withdrawal rate simulation curves for distribution. In order to set yourself up for the ability to take higher retirement income rates safely, it is necessary to introduce another economic power that specializes in distribution, which is actuarial science. These two powers for accumulation and distribution are meant to work together to create higher retirement income. So the question is how can we introduce this actuarial science power into our long term wealth building?

SLIDE 41
The answer is through permanent life insurance, specifically whole life insurance. Then the power of actuarial science, through the death benefits and cash values of the whole life insurance, can interact with the interest rate power of retirement assets to create the ability to take higher retirement income rates safely. We need to be working towards building the proper balance between these two powers on our way to retirement. Let's go through how these two powers can work together.

SLIDE 42

The interaction of these two cornerstones provides both the exchange/trade option which we call the Covered Assets, and the investment option which we call the Volatility Buffer to choose from at the time of retirement. You are not locking into which option or options you will want to utilize in the future today. The fact that you have built these two cornerstones together gives you the ability to choose from one, or combine the options together at the time of retirement for income. Let's go through both of these options.

SLIDE 43 *(Ask client(s) to read this slide.)*

Option one is called "covered retirement assets". A covered retirement asset is one that is accompanied by an equal amount of whole life insurance death benefit. Similar to how most government entities provide retirement pensions to their employees, covered retirement assets lay the foundation for self-made pensions in retirement. This is accomplished through the interaction of a retirement income tool that is unrelated to the curves of the withdrawal rate simulations called an income annuity, a self-made pension, and your whole life insurance death benefit. Under this option the interaction of your retirement assets and whole life insurance death benefit gives you the ability to create a guaranteed retirement paycheck for life historically in the range of seven to thirteen percent from the assets you've built, while at the same time providing perpetuation of retirement income for a spouse and or a legacy for your heirs. The closer you get to having the same amount of retirement assets and whole life insurance death benefit at retirement time the more covered assets you have and the higher your retirement income can go.

SLIDE 44

Visually, this is how this would look. On the left side in pre-retirement we put all of our savings towards building retirement assets only. Let's say they could accumulate a unit of money that we will call a million dollars here. At retirement time along this path, we would have set ourselves up for withdrawal rate simulation income at that time somewhere between three and four percent so we'll call it three and a half percent of the million dollars, that's thirty five thousand dollars a year of non-guaranteed retirement income going down that path. On the right side, we are going to take the same amount of annual savings in pre-retirement that we had on the left side, but now we are going to split it between building retirement assets and whole life insurance. We are not going to end up with the same amount of retirement assets that we did on the left side because we are splitting where we are putting our annual savings every year. So you have seven hundred and fifty thousand of retirement asset value and seven hundred and fifty thousand of whole life death benefit with two hundred and fifty thousand dollars of cash value. So now what we get to see is the interaction between the death benefit of the whole life insurance policy and how we can use our retirement assets to create much higher income streams. Since we know that we'll have seven hundred and fifty thousand in death benefit the day someone passes away, this allows us to take the retirement assets we have and trade them for a self-made pension on that person's life. This is called an income annuity. You are physically trading this to an insurance company in exchange for a guaranteed income stream for life, which for a sixty five year old male has averaged around ten percent as an income annuity rate. Once that rate is set, it doesn't fluctuate. In this case we have seven hundred and fifty thousand being traded for a guaranteed seventy

five thousand dollars a year of income for that person's life. Now, when that person passes away, that income stream stops and the retirement asset that was traded for that income stream is no longer there. Then the death benefit for the whole life insurance policy kicks in to replace the retirement asset that was originally traded to create the initial income stream. The remaining spouse can use that death benefit to recreate that same income stream or maybe it's just a legacy at that time for heirs or charities. This is how the covered retirement asset option works. In this example, you have seventy five thousand a year guaranteed retirement income versus thirty five thousand dollars not guaranteed.

SLIDE 45 *(Have the client(s) read this slide, and highlight the phrase in bold and underlined below. There are only two options for us to get income in retirement, trading or investing. We aren't trying to choose one of these options today and we don't want to pigeon hole ourselves. We want to put ourselves on a path to have the choice between these in the future on the highest spectrum.)*
This brings us to option two, "Volatility Buffer". Remember, we are not choosing one of these options today. Getting these cornerstones in place gives us the ability to choose between these options later on at the time of retirement. So let's read through option two. **If you choose not to create self-made pensions with your retirement assets for income as discussed in option number one, then your retirement assets will need to be invested to create your income.** However, taking income rates in the range of seven to thirteen percent from your invested retirement assets gives you high probabilities of running out of money based on regular withdrawal rate simulations. The reason this occurs is because a primary assumption of the simulations is that you have to take your income from that pot of money every year, never giving it a break. To avoid running out of money, a key to taking high withdrawal rates in the range of seven to thirteen percent from invested assets is to not always have to withdraw your income from this pot of money after a year in which your asset base did not earn what you were going to pull out. This gives your asset base a volatility buffer year and a chance to recover. After some of the years in which your asset base did not earn what you were going to pull out you would need the ability to withdraw your income stream from a different asset that is not significantly affected by short term interest rate swings and market fluctuations. The cash values of your whole life insurance policy can fit this bill. Having years of retirement income available in the cash values of your whole life insurance policy is vital in retirement if you choose to invest your money to create retirement income.

SLIDE 46
Visually, we have the same set up. On the left side, without cornerstones, we have a three and a half percent withdrawal rate simulation which gives us an income of thirty five thousand dollars a year from our retirement assets. On the right side we have the cornerstones; retirement assets and whole life insurance. Now what we're going to do instead of trading our money to get our retirement income streams, is invest the seven hundred and fifty thousand dollars of retirement assets and pull money off to get our retirement income streams. We are going to pull a higher income rate than what withdrawal rate simulations would normally say is prudent from a probability standpoint because we know we have the ability to also pull income from the cash values of the whole life insurance policy as a volatility buffer. The way this works in this case is we have a ten percent withdrawal, which is seventy-five thousand dollars a year. At the beginning of year two I look back on year one's return to see if I earned the seventy five thousand dollars that I pulled out of that asset. If I did not, I would give that asset a

break. Then pull the income the next year from the cash values of the whole life insurance policy that aren't as significantly affected by short term interest rate swings and market fluctuations. I do this as many times as I need to, or can.

SLIDE 47

Let's take a look at an example illustrating the effectiveness of the volatility buffer when withdrawing high income rates from invested money. To do this we have to look at the results of pulling income from the $750,000 during a time frame without a volatility buffer first and then compare that to what it would be with the volatility buffer.

SLIDE 48

So what we see here on the left side, is the beginning retirement asset value of seven hundred and fifty thousand dollars from the cornerstones example that we were just looking at. This side is without a volatility buffer so we are going to be pulling ten percent income from that beginning value which is seventy five thousand dollars a year every single year during a period that averaged twelve point seven seven percent. When we do this every single year, we run out of money between years thirteen and fourteen which is fairly consistent with regular withdrawal rate simulation probabilities at higher income rates. Now when we go over to the right side, we are going to demonstrate the power of the volatility buffer in the cash value of the whole life insurance policy. So we have the same setup, but now after years in the beginning when we did not earn what we pulled out, we are going to give this asset a break and not draw our income stream from here. Instead, we will draw from the cash values of the whole life insurance policy which are not as significantly affected by the short term interest rate swings and market fluctuations. So we see here in year two, we look back on your one's return and we see it had a positive return, but we didn't earn the seventy five thousand we pulled out that year. Then in year two, instead of pulling our income from this invested pot of money, we pulled the income from the cash value of the whole life insurance policy instead, giving this asset a break and a chance for the retirement asset values to recover. We are trying to preserve these workers here. Think of all of these dollars over here as your workers. We want to preserve these workers, we don't want to be killing them off and that's what the volatility buffer in the cash value of the whole life insurance policy allows you to do with the retirement assets that are invested. And we use the volatility buffer as needed as many times as we can. You will generally get between 3-9 years of volatility buffer in the cash values for what you have balanced in the Covered Assets strategy. In this example we used it three times based on what was available in the cash values. And you can see the power of this as far as what happens with the account value instead of running out of money between years thirteen and fourteen on the left side, we now have more money than we started with twenty years down the road on the right side. **Remember though that in the world of fluctuating returns measuring the results of one time frame is not conclusive. What you'd need to do is run thousands of simulations throughout history to determine probabilities of not running out of money based on various withdrawal rates incorporating years of volatility buffer.**

SLIDE 49

This is the regular withdrawal rate simulation chart that we looked at before that doesn't include any years of volatility buffer. In the next few slides watch what happens to the probabilities of the different withdrawal rate curves as we incorporate the Volatility Buffer strategy with years of buffer included in the simulations.

SLIDE 50
This is the withdrawal rate simulation chart for the Volatility Buffer strategy with 3 years of buffer.

SLIDE 51
This is the withdrawal rate simulation chart for the Volatility Buffer strategy with 4 years of buffer.

SLIDE 52
This is the withdrawal rate simulation chart for the Volatility Buffer strategy with 5 years of buffer.

SLIDE 53
This is the withdrawal rate simulation chart for the Volatility Buffer strategy with 6 years of buffer.

SLIDE 54
This is the withdrawal rate simulation chart for the Volatility Buffer strategy with 7 years of buffer.

SLIDE 55
This is the withdrawal rate simulation chart for the Volatility Buffer strategy with 8 years of buffer.

SLIDE 56
This is the withdrawal rate simulation chart for the Volatility Buffer strategy with 9 years of buffer……. So this is the Volatility Buffer, Option #2.

SLIDE 57
Again, the decision for which option or combination of options to use for retirement income is made at the time of retirement. But no matter which cornerstones option you choose, you are much better off than being relegated to an invested retirement asset only strategy for retirement income. So it's vital to have these two cornerstones working together giving you the ability to create potentially higher, more secure retirement income streams. So start building your cornerstones together as soon as possible to allow them both the time to build and grow. The big picture strategies you implement today, directly impact your retirement income later. Time is of the essence.

SLIDE 58
What we've done is economically defined the three areas of allocation savings for efficiency. We have one short term area, and two long term wealth building areas. So it is vital to be building the proper balances between these three areas to get the most out of your wealth building in pre-retirement and also set yourself up for the biggest retirement income streams later.

Chapter 4: Implementation (Cornerstones Calculator Summary Examples)

SLIDE 59 *(you can show one or both of these Cornerstones Calculator Summary output examples)*
What you see here is an example summary output of our Cornerstones Calculator for a 40 year old couple. This calculator compares the retirement income calculations for building Retirement Assets only and ending up with 3-4% retirement income rates, the salmon color, to the Cornerstones Strategy options of Covered Assets and Volatility Buffer, the blue and green colors, using the exact same assumptions and same amount of savings in each scenario going forward. At our next meeting we can use this calculator to run your own retirement income comparison calculations based on these different concepts and strategies we've just discussed using your current savings. This calculator does two things for us: First it will help us compare the efficiency of the different strategies for you, and second it will give us a marker for what your retirement income might be in the future based on the assumptions made. This will help us determine how you want to be allocating your money today and how much you want to be saving today. To be able to run these calculations though we need to know what you might qualify for with regard to the Whole Life Insurance, because you can't just get Whole Life Insurance, you have to be underwritten for it by an insurance company. The underwriting process usually takes between 3-6 weeks. What I'd like to do with you today is get you into the underwriting process by filling out an application to get this process started. You're not buying or committing to anything today, we're just asking the insurance company for an underwriting classification for you. Then while this process is going on behind the scenes we can get back together in a week or two to run through your own calculations. How does this sound to you?

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