

Retirement Income and Distribution Planning: *eMoney Advisor* *Excerpted Profile*

Note: This authorized reprint contains material excerpted from the Celent report: Retirement Income & Distribution Planning (February 2008). The full report is 78 pages in length and contains profiles of fifteen major planning software vendors, including eMoney Advisor. This report was not sponsored by eMoney Advisor in any way. This reprint was prepared specifically for eMoney Advisor, but the analysis presented has not been changed in any way from the data presented in the full report.

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Editorial Team

Author: Robert J. Ellis

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Celent

745 Boylston Street, Suite 502
Boston, Massachusetts 02116
USA

Telephone:
+1.617.262.3120
Facsimile:
+1.617.262.3121
Email:
info@celent.com

www.celent.com

Author:

Robert J. Ellis
rellis@celent.com

Executive Summary

Retirement distribution and income planning has been described as “the missing link of financial planning” for mass affluent and high net worth households in the US. Until the last year or so, financial planning has almost exclusively focused on the accumulation phase of the individuals’ and their household’s life span, leaving a complete blank in most financial plans when it comes to the variety of important decisions that investors must make as they approach retirement and after they retire. These decisions can make the difference between a quality retirement with plenty of assets and security and an uncertain retirement with unnecessary worries.

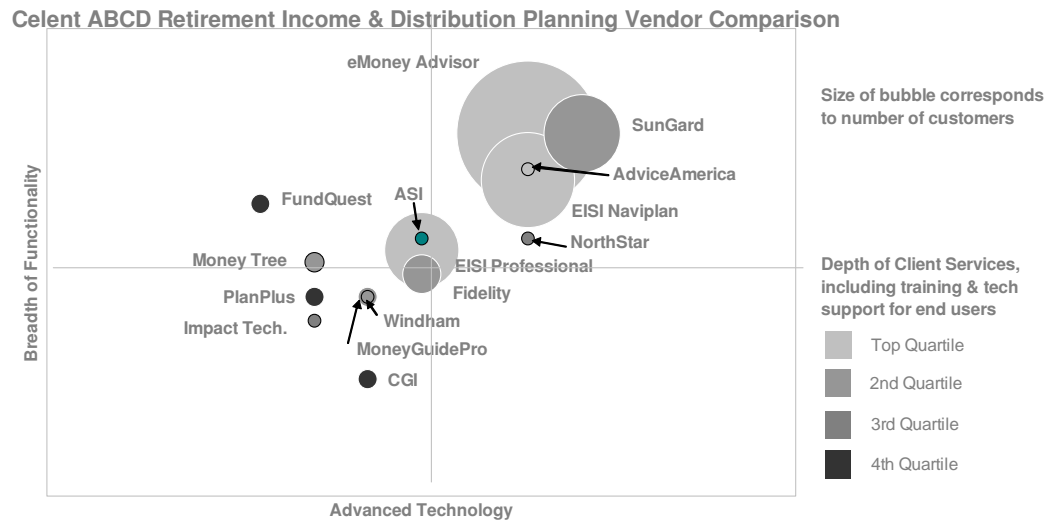
Neglect of post-retirement income and distribution planning has occurred for many reasons. Cynics have ascribed it to the fact that financial planners and advisors get paid significantly less when assets are declining, and retirees are being more careful with their investment selections in terms of costs and commissions. More astute advisors have noted the paucity of tools available to advisors to handle this stage of their clients’ lives. Complex decisions about Social Security, specification of which accounts will be liquidated in what order, tax issues, and new post-retirement investment products have all made the financial planning community loath to tackle the problem head on. However, new tools and greater attention to the situation from both insistent baby boomers and the media are improving the situation.

This report begins with an introduction to retirement income and distribution planning. Following that, the report discusses why this area is important to financial planners and their clients, and then explores in depth how the distribution phase is fundamentally different from the accumulation phase.

After reviewing the unique aspects of retirement income and distribution planning, this report looks at the eMoney Advisor tools available to support the financial advisor as he or she guides the client through the decisions that must be made in the post-retirement life phase.

This technology is then evaluated in a series of tables and in Celent’s ABCD Vendor View. The ABCD Vendor View portrays at a glance the relative position of vendors based on the following categories: **A**dvanced Technology, **B**readth of Functionality, **C**ustomer Base (number of paying clients), and **D**epth of Client Services, and is graphically presented in Figure 1 on page 5.

Figure 1: Celent ABCD Retirement income and Distribution Planning Vendor Analysis



Source: Celent

Following the Celent ABCD Vendor View, the report takes a look at the future trends of retirement distribution and income planning. The report finishes with some conclusions about the future of the post-accumulation phase of financial planning.

Introduction to Retirement Income and Distribution Planning

The North American wealth management industry has been primarily focused on asset accumulation for much of its history. “Increase your investments for a better future,” the clients are told by their financial advisors. “Gather more assets,” the brokers and planners have been ordered by management. “Save more,” the government tells us as the safety net of Social Security shows more rips and strains. At the end of the day, firms and advisors were evaluated on a single metric: client assets under management. Clients kept their own personal score by the same metric.

The accumulation mantra was fine while the massive cohort of baby boomers (born from 1946 to 1964) was still in the pre-retirement phase. But beginning in 2008, the 73 million baby boomers will have started retiring, or at least qualifying for Social Security. In fact, many of the boomers have actually begun their retirements a few years ahead of eligibility for Social Security. According to Cerrulli Associates, the assets held by those already retired in 2012 will total more than US\$19.5 trillion.

All of a sudden, beginning in 2008, assets for the boomer cohorts were no longer being generated by employment. Instead, boomers have begun to draw down on their, in some cases, substantial assets already gathered and saved in a variety of accounts; joint investment accounts, IRAs, Roth IRAs, 401ks, Keoghs, and the like. The few fortunate enough to be covered by a defined benefit pension plan (21% of the private sector and almost 100% of the public sector) began receiving their payments, with the eventual kicker provided from Social Security. Further complicating departure, but adding real value for the lucky few, were vested options and the transition proceeds from ownership of a business venture.

This move from accumulation to distribution has had some interesting consequences for the investors.

- At the point when the retiree needed significant advice, the financial advisor was losing interest in serving the client. After all, the advisor had gathered as many assets as they were likely to get. Fees were declining; how could they provide more and complex services now?
- Financial planning models and tools, for the most part, only got the advisor and client to the point of retirement. Distributing (or “de-accumulating” in the unfortunate parlance of some systems) the assets was rarely discussed in detail. The average age of retirement is now 62 (up from 60 in just the past 10 years) and expected to go higher on average, wholly driven by those who lack significant retirement assets and must keep working.
- Significant tax implications occur based on what accounts were liquidated first, plus the age of distribution is also forced for some types of retirement

accounts. Some analysis shows that poor tax decisions in retirement can halve the annual income of a retiree.

- Decisions about such mortal subjects as longevity and health, not to mention heirs and bequests, began to weigh heavily on the process. For married couples aged 65, there is an 83.7% (better than four out of five) chance that one spouse will make it to 85, a 63% (better than three out of five) chance of making it to 90, and a 35.7% (one out of three) chance of making it to 95. That means that retirement horizons should now be 30 years and greater, at a minimum.
- Distribution decisions are highly sensitive as to the expenses of living, as well as the cost of living in terms of inflation.
- Poor distribution decisions, combined with the lack of assets to distribute, have also resulted in many retirements being deferred or even canceled as older workers are forced back into the job market.
- Financial planners have now become life coaches as potential retirees ask, "When can I retire?" These individuals are looking for time-certain retirement dates, but planners must also help them consider the options of part-time employment or employment in different fields.

When asked by *Financial Planning* magazine how many financial advisors offered "retirement income planning," a resounding 92% said they did. But a deeper dive into the systems used and the plans developed indicate that very few went beyond a simple "you'll need this many assets to fund this much income in retirement" approach.

Facing this brave new world, only a few financial advisors, financial product developers, and planning systems vendors have really stepped up to deal with the complex issues of post-retirement income and asset distribution. Part of the problem is that given the complexity of issues, and lacking appropriate platform tools, the financial advisor is just not prepared to address the issues. Another part of the problem is the uncomfortable nature of discussing mortality and failing health with clients, especially as the advisor almost always wants to be seen as nice and friendly in order to have, and thereby retain, a happy client.

However, as with most things in life, failure to deal with issues now can only have worse ramifications later. It would not be inconceivable that, as the boomers begin to retire and find they have financially constrained lifestyles, they will turn to that other booming industry, litigation, and go after their financial advisors for failing to help them prepare for the last 30 to 40 years of their lives.

Why Is Retirement Income and Distribution Planning Important?

Assets for Retirement

Retirement distribution and income planning is a vital topic that will get more and more attention over the next few years as 73 million baby boomers enter retirement, putting US\$19 trillion of assets, \$12 trillion of which are in currently qualified retirement accounts, into play. If firms are not ready to advise on the distribution phase, and to build an appropriate business model that rewards the financial advisors while creating a good value proposition for the clients, they could see a considerable outflow of assets.

These assets are expected to grow to nearly \$30 trillion before they start to decline in total through distribution and expenditure, according to a FundQuest white paper, *A Process-Centered Approach to Retirement Income*.

The assets held by the boomers approaching retirement are not evenly distributed. While the boomers' net worth equals 70% of the net worth of all households in the US, the average boomer household in 2005 had only \$49,944 saved for retirement (US Department of Labor). Even scarier, the median amount of retirement savings for the boomers was around \$2,000. The average total financial assets for the boomers was just over \$100,000, with average non-financial assets just over \$250,000, most of which represented the value of highly leveraged homes. With the same skewing effect that high-asset households have on the averages, the median assets are significantly lower. (For more details, see Table 1 on page 9.)

Table 1: Available Assets for Retirement (US\$)

Age in 2004	Years to Retirement (est. @ 65)	Average Net Worth	Average Financial Assets	Average Non-Financial Assets	Average Household Income
Under 35	30+	\$12,300	\$3,700	\$16,300	\$33,887
35–44	20–30	\$97,790	\$23,000	\$161,600	\$58,532
45–54	10–20	\$368,075	\$105,000	\$335,850	\$92,419
55–64	0–10	\$808,200	\$288,100	\$562,750	\$108,849
65–74	NA	\$703,900	\$255,800	\$372,700	\$63,666
75 and up	NA	\$437,900	\$144,000	\$216,000	\$40,048

Source: Federal Reserve Board, Survey of Consumer Finances (2004), Celent analysis

Equally scary, of those households with retirement assets, only 50% are estimated to have a financial plan that evaluates current savings and the assets needed at retirement. Less than 5% have a plan that covers retirement distribution and income planning.

Retirement Risks

Retirement income and distribution planning are vital to help pre-retirement families face the following post-retirement risks:

- Longevity Risk.** It is necessary to ensure families don't outlive their assets. A couple of 65-year-olds has a 50% chance of having one of the two live until they are 92. An individual has a 50% chance of making it until 85. Either way, on average, half of all retirees need a post-retirement plan that considers a 30+ year retirement horizon. A 40-year post-retirement plan is not out of the question for some healthy retirees. To put that in perspective, the post-retirement distribution phase is as long as the entire working, or accumulation, phase.
- Healthcare Cost Risk.** Current predictions from Fidelity assume that a retiring couple will need \$200,000 throughout the remainder of their lifetime just for health-related expenses. Long-term care can add another \$130,000 to that number for the projected three years for one of the two in the couple. The alternative is to spend down on current assets early to acquire appropriate long-term and nursing-home insurance, which is not an inexpensive option and utilizes savings assets.
- Return Risk.** The entire financial planning process is highly dependent on projected rates of return. However, with no new accumulations to replace shortfalls, an under-performance in returns can have a devastating impact

on monthly incomes and cause a more rapid drawdown in investment assets.

- **Tax Risk.** A bad distribution plan will incur unnecessary tax expenses. These expenses can rapidly add up to a significant portion of the entire retirement asset pool without careful planning. Taxes are one area where the plan has to be frequently revisited to ensure there have been no changes in tax assumptions and rates.
- **Market Risk.** A distribution and income plan must take into account volatility in markets, especially if a market drop is concurrent with a need for the assets. Overall, a client in the post-retirement distribution phase is less able to handle a significant market drop because they have less time to rebuild their portfolio. Modeling is one of the best tools to ensure that a portfolio can survive a severe market drop.
- **Inflation Risk.** Inflation over time is the killer of portfolios, unless the portfolio has been inoculated against inflation risk. Forty years of inflation at 8%, not an unreasonable actual measure of the change in costs in healthcare and other senior consumables, reduces the value of \$1,000 at retirement to \$46 of purchasing power in the last year of life!
- **Excess Withdrawal Risk.** Heavy spending, especially at the beginning of the retirement disbursement stage, will raise the probability of not having sufficient funds at the end. For example, a couple looking at their million dollars of investments may think that a \$200,000 40-foot Hatteras would be a great thing to have, and they are pretty certain they can afford it. However, the impact of the boat on their next 40 years of retirement could be extreme. In addition to the lost earning power of the \$200,000, there will be increases in expenses for fuel, slip rentals, insurance, licenses, and maintenance. The financial impact could easily be a reduction of 40% to 60% in their future living standard.

Fidelity Investments estimates, by using statistical modeling (with a 90% certainty), that a withdrawal rate of 10% will eat through the client's portfolio in just 11 years, a 6% withdrawal rate in 21 years, and a 4% withdrawal rate in 33 years. Given that some may need to plan for a 40-year planning horizon, a 3% to 4% withdrawal rate appears to be the optimal for a retirement income planning scenario. However, more sophisticated planning tools are now eliminating the fixed withdrawal percentage in favor of more time, return, and inflation-sensitive amounts.

- **Unplanned Events Risk.** No matter how good the financial plan, death and illness, market reversals, or other losses all may occur in a manner to impact the retirement asset pool. While modeling and insurance can help, there are no guarantees in life, or retirement portfolios. This is one further reason that a retirement distribution and income plan cannot be "file and forget," but must be continuously reviewed with a trusted financial advisor.

Retirement Investment Products

Good retirement distribution and income planning cannot be solely reliant on a product-based solution, though certain products will have key roles in retirement distribution and asset planning. These retirement-focused products include immediate, deferred, fixed and variable annuities, target date and lifestyle mutual funds, plus long-term care and life insurance. It is likely that, with such a large pool of assets available for transition, product developers will continue to create new products, and products such as reverse mortgages, bond and annuity ladders will gain more traction. The product descriptors to look out for are “guaranteed income” and “guaranteed principal”; those phrases identify the target audience for retirement products. Retirement and distribution-based products are discussed in more detail on page 14.

Retirement planning requires an ongoing process of advisement, coupled with good technological tools and appropriate products, to guide the client through their long retirement phase.

Social Security

No report on retirement income and distribution planning covering the US is complete without a discussion of Social Security. Social Security represents a significant source of monthly income for even former high-earners, and a safety net for those with little or no assets.

The big unknown with Social Security is when, after retirement, the retiree should begin to receive benefits. Up until age 70, the longer one waits, the larger the monthly benefits one receives. In general, for each year one takes benefits prior to “full benefits,” one’s monthly payment is reduced 6%. Each year after one’s “full benefits” date is worth an 8% increase in the monthly amount. And benefits are adjusted for inflation.

However, the longer one waits, the more one must rely on other assets. The Social Security Administration is even nice enough to put a “break-even” calculator on its website telling a potential retiree how long they have to live to come out ahead with earlier or later benefits. The idea is that the citizen guesses (or gambles) that they will live longer or shorter than the break-even life expectancy.

However, the calculator fails to take into account several factors, and it is here where the financial advisor adds value when discussing Social Security with their client:

- What are the expected financial gains from taking benefits earlier and investing them?
- What are the financial penalties from not taking the benefits and utilizing current investments, including tax consequences?
- What is the likelihood for people to overestimate or underestimate their life expectancy?
- The age and health of the spouse, and which person was the higher wage earner, impact the step-up to the higher benefit and overall life expectancy in terms of the death date of the surviving spouse.

- What is the likelihood that full benefits will continue to be pushed back to ensure the program's solvency?
- What are the guarantees that the US Government will be willing or able to continue to pay the benefits to the retiree at the projected level, or even at all, in the case of wealthier clients?

The average of retirees taking Social Security "early," despite the entire population working longer, has increased. In 2005, with full benefits available only at 66, 85% took early reduced benefits. In 1999, when full benefits were available at 65, 66% of men and 71% of women took early benefits. Clearly, despite an overall rise in average wealth levels, the mass of the populace believe that they are financially ahead by taking the benefits early.

As of yet, there are very few planning tools that do a good job integrating the complex issues associated with Social Security.

How Is Planning for the Post-Accumulation Phase Different?

The 10 Factors

There are 10 differential factors for planning through retirement as far as retirement income and distribution planning is concerned. The following list outlines those planning agendas in the order they need to be considered when evaluating both a retirement income and distribution plan, or the planning platform that such a plan must be constructed upon.

Factor 1: Retirement is no longer a period of inactivity or passivity for the investment portfolio is concerned. Given that a retirement time frame can be up to 40 years long, the idea that one can set one's portfolio at retirement, or even five years before retirement, and forget it is not intelligent or wise.

Factor 2: Risk over 40 years must be handled appropriately. Inflation risk requires an exposure to inflation-protected assets, whether they be equities, TIPS, variable annuities, or real estate.

Factor 3: Retirement distribution and income planning requires a focus on return of investment as well as return on investment, so insurance products also gain more traction with both the advisor and client. That in turn requires a planning platform that actively incorporates insurance products.

Factor 4: Income planning throughout the remaining lifetime brings significantly more focus to annuity-based products. Annuities are the products that best mimic the benefits of the now long-lamented defined benefit pension plan. Income planning also requires matching assets possessing a high level of certainty (e.g., Social Security) greater than the variable income sources (e.g., variable annuities), then adding increased certainty through other annuity-type products.

Factor 5: Distribution planning is vital. Not all accounts are equal, especially in the eyes of the tax man. There are taxable and tax-free distributions, partially taxable distributions, and long-term and short-term gains, all within taxable or qualified accounts. A bad decision can wipe out 40%+ of the available retirement income; it can also incur penalties (for example, in the case of failing to take minimum required distributions from certain types of accounts).

Factor 6: It is not only the income taxes one has to plan for. Given the size of the client's estate and the vagaries of US (and to a lesser extent, Canadian) tax law, failure to take into account estate taxes by properly utilizing spousal deductions and beneficiary designations can be a very expensive error. Furthermore, in today's world, international assets (e.g., that retirement villa in Honduras purchased so inexpensively all those years ago) may also incur complex estate tax ramifications in remote jurisdictions.

Factor 7: The client's retirement income and distribution plan cannot be created in a vacuum. The post-retirement piece is just part of a larger financial plan, which is itself in turn part of an even larger life plan that reflects goal, career and compensation levels, educational plans, and the health situation of the clients.

Factor 8: Neither can the retirement income and distribution plan be created and filed. The plan requires regular re-evaluations to identify changing circumstances, and the changing desires of the clients. Changing asset values should be regularly reflected in the plan.

Factor 9: More and more clients are becoming self-directed in some or all of their investment decision-making. That is, in and of itself, a good thing because advisors could not serve as many clients if they had to constantly meet and work with them all. However, it also means that clients need access to their information when they have decisions to make, which means web access to their plans, hopefully updated for asset values on a regular (read: at least daily) basis.

Factor 10: Another interesting aspect of post-retirement planning is the importance of the family budget. While all clients know that a budget is a basic financial housekeeping item, few prepare them and even fewer adhere to them. Most clients feel that they don't make large impulse purchases and that they are credit smart. The good news is that, during the accumulation phase, spending mistakes can be rectified. Once into the post-retirement phase, spending errors have much more dire consequences. The financial advisor has an obligation to help the client build and adhere to a budget.

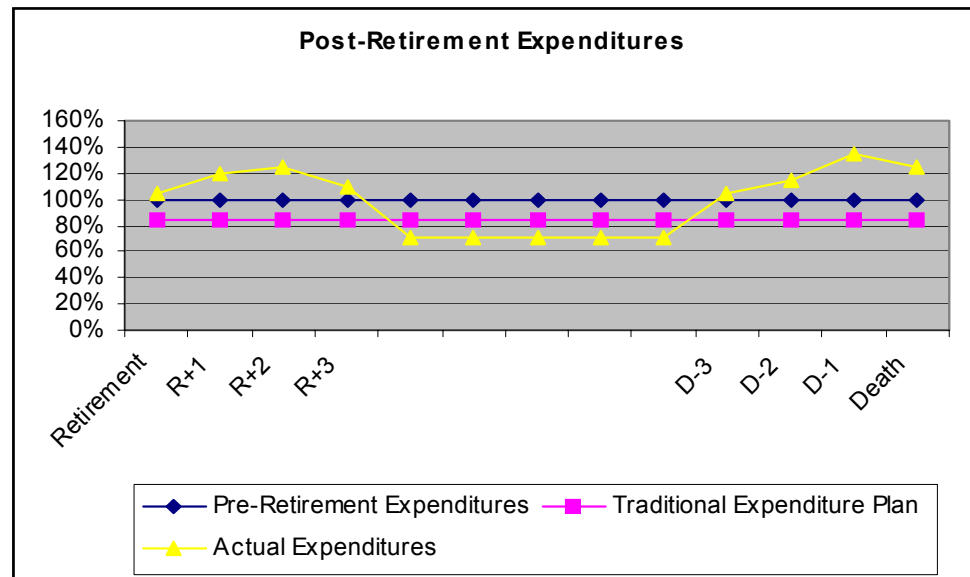
Retirement Needs

Many retirement systems look at living expenses that are a flat percentage of pre-retirement income. Numbers used range from 70% to 85% on average. This is the wrong way to look at living expenses for the retiree.

Figure 2 on page 15 is a retirement expenditure graph based on research done by the author in 2001. It shows the expenditures of retiring clients over time versus their pre-retirement living expenses. (Note: the planner should always look at living expenses, not income, because the client will no longer be saving for retirement, but they must include taxes.) During initial years of retirement, the retiree couple actually spends more than they were spending prior to retirement. The reasons; they now have more time on their hands, and they fill it by playing more golf, traveling more, buying that waterfront vacation condo, etc. The study indicated that, on average, retirees' expenditures peak in post-retirement years two and three at around 125% of pre-retirement expenditures, then over the next few years, decline to about 80% of the former level.

They continue at this level until the post-retirees hit the big unknowns, health and death. About three years prior to death, expenditures zoom back up well above the former expense level, sometimes to as high as 150% to 200% depending on the severity of illness and the needs for nursing care. Fortunately, these expenditures can be offset by insurance and long-term care insurance benefits. It is the exceptional planner and planning system that takes into account these variations in post-retirement living expenses.

Figure 2: Post-Retirement Expenditures vs. Pre-Retirement Living Expenses



Source: Celent analysis

The Post-Retirement Products

Certain products offer specific advantages in the post-retirement phase of a client lifetime. These products are more often than not acquired for their retirement income capabilities as opposed to pure accumulation, and it is vital that any planning tool focused on the post-retirement phase be able to take them into account and optimize their usage.

High taxes and asset management fees can destroy an investment portfolio in retirement. The best financial retirement products fulfill what Harold Evensky, the legendary financial planner, calls the “paycheck syndrome.” Evensky maintains that most Americans are used to a regular and dependable paycheck, and that they are seeking the same thing in retirement. Evensky further maintains that reliance on dividends and interest, which can fluctuate significantly over a 30-year retirement, does not solve the “paycheck syndrome.” Evensky seeks to provide his clients with financial security through a total return strategy with minimal volatility, not portfolios constructed using modern portfolio theory. Supporting Evensky are studies that indicate that a regular payment during retirement increases the satisfaction with retirement more than drawing down on even substantial assets.

If a financial advisor is constructing a client portfolio for total return, they must also take into account the timing of cash flows, not just absolute returns. Evensky assumes returns on equities of 6%, just half the historic returns of the last 20 years. To get the desired

return, Evensky focuses more on taxes and asset management fees, utilizing **ETFs and indexed mutual funds**. Only for a small portion of the portfolio does Evensky introduce risk, higher returns, and active management.

Annuities offer several advantages when planning a post-retirement income scenario. It is not the annuity itself per se, but the ability to receive a stream of revenue from an asset (annuitization) that is the key, helping the retirees avoid “paycheck syndrome.” Annuitized cashflow streams can be received from both variable and fixed annuities (both immediate and deferred), as well as whole life and other life insurance products with cash value.

Annuities, based on mortality tables, allow for period-certain or lifetime payments to the annuitant. In this regard, they can be used as a surrogate pension for those people not covered by traditional defined benefit pensions. There is a great psychic value to clients knowing that they cannot outlive this stream of income if they take payouts in the form of a lifetime payment. This psychic value, especially as the planner has just scared the client about outliving their money, often steers clients to select the annuity option.

Long-term care insurance is another post-retirement planning product that is more often than not sold on the basis of fear. (By the way, all financial products are sold based on either fear or greed, the only two motivators.) It is true that one out of two people will wind up in a nursing care facility for on average two to three years, and that nursing costs are rising significantly. In fact, in many parts of the US today, daily costs now exceed \$300. Two years of care will therefore run over \$200,000. With an 8% inflation rate at the end of a 30-year retirement, that nursing care stay will cost \$2.2 million!

The problem with long-term care insurance is that it is expensive so it eats into current assets, which reduces future income flows. Second, the rates are not fixed, so it is not unusual for insurance companies to find they have underpriced their risk and raise rates 10% or so every couple of years. Lastly, some firms simply exit the business and don't write anything but the renewals they are obligated to write.

Life insurance is the traditional tool for protecting widows (and widowers) and heirs. It can be paid in a lump sum or in an annuity, and like most other post-retirement products, is based on mortality tables. Mortality tables represent nothing more than the bet that you die before or after the insurance company thinks you will. With life insurance, counter-intuitively, the longer the insured lives, the more the insurance company wins, unlike reverse mortgages and lifetime annuities.

Reverse Mortgages are slowly gaining ground as valuable post-retirement tools. They represent the distribution of the equity built up in a residence or vacation home. While this equity can be released by other methods, such as a home equity loan or line of credit, only a reverse mortgage ensures a lifetime income flow and no liability after death. Homeowners can tap into them as early as age 62, but are currently limited to one property with the federally guaranteed program.

While the product has been around for at least a decade, only within the last couple of years have planners started to seriously consider reverse mortgages as part of a post-retirement income plan. One of the reasons is the lowering of costs, and the easing of

rules by the Federal Government on federal insurance for the product. Fees are still around 4% for origination and the insurance component, but increased competition is putting downward pressure on fees. To date, less than 1% of all private homes in the US have had reverse mortgages placed on them, and the current customers skew heavily to older women without other significant sources of income.

The year 2006 had 76,276 federally insured reverse mortgages created, representing 90% of the market. (Private reverse mortgages are usually done for “jumbo loans” above the \$362,790 urban federal limit and for second homes.) Some of the more sophisticated strategies use reverse mortgages to pay for long-term care insurance, because at that time, the house will no longer be needed and can be sold.

Fidelity has recently created **Income Replacement Funds**; mutual funds that self-liquidate on a pre-determined schedule. These liquidations provide the income for the asset holder without tying up the assets in an annuity. Like the lifecycle accumulation funds, these funds gradually switch their allocation from equities to bonds as the liquidity event nears. It is too soon to know how these funds will be received by the mass affluent clients they are designed to serve.

The “Letters” Explosion

In an attempt to capitalize on the growing need for retirement and distribution planning, a variety of specialist planner organizations are springing up. Claiming that they are experts in the planning needs for retirees, these creative minds have invented a handful of professional designations based on the pretense that only specialists with their approved designations can deal with the issues of distribution planning. The two largest of these are the “RFG” (Registered Financial Gerontologist) and the “CSA” (Certified Senior Advisor).

These new designations are a natural outgrowth of the 25-year-old non-governmental designation of CFP, Certified Financial Planner. By creating a non-governmental, non-licensed designation that implies a greater level of expertise than that of the non-designated individual (who may, in fact, may have superior legal credentials), the financial planner seeks to differentiate themselves from the crowd, and not incidentally, gain more clients and charge higher fees.

Clients don't need these newer experts with their multiple designations. In fact, by selecting them, they may find that their plan has overlooked such basics as tax impact. Clients are better off with licensed professionals, or at least a CFP. An experienced financial advisor with appropriate technological tools can do a better job for their clients than a newly minted specialist who has paid several thousand dollars for a few classes and some letters for their business card.

Tools for Retirement Income and Distribution Planning

In the area of retirement distribution and income planning, many vendors are realizing that their tools are insufficient for providing the financial advisor with appropriate guidance and advice for the ultimate client.

Celent has identified the following key capabilities for a system of model to be considered as adequately serving the space. These tools include:

- A model that looks at income from all sources, not just the retirement assets saved. These include Social Security, defined benefit pensions, reverse mortgages, annuities and liquidation of business assets.
- Tax planning that takes into account nature of different types of accounts.
- Traditional modeling tools, including cash flow analysis and Monte Carlo type simulation to generate certainties of outcomes.
- Integration with traditional planning tools utilized during the accumulation phase of the planning process.

eMoney Advisor

eMoney Advisor's 360 and 360 Pro planning platforms both contain a retirement planner as one of the six main planning modules, plus a stand-alone Retirement Income Tool. The 360 system is aimed at Registered Reps of broker-dealers, while 360 Pro is aimed at the high-end planning market where the advisor can be properly compensated for their guidance, specifically, the mass affluent and high net worth segments.

The two systems have similar functionality in terms of planning approach, though the 360 Pro offers more add-on capabilities in the Planning Center, where specialized tools for estate planning and long-term care can be found. Both systems seek to identify decision points for clients, and at the appropriate point, bring the client into the discussion as to aspects that effect their post-retirement scenario, specifically:

- How much should we spend?
- Are we OK with the level of risk we are taking?

Both 360 and 360 Pro adopt a client educational tone and presentation format. Each page of analysis that will be included in the final report, based on either a firm's or advisor's selection, contains extensive text and illustrations. Pages and even some specific paragraphs can be eliminated or included based on client need levels and compliance approval.

On the interactive screen, and included in the report, are a series of single number alerts for such aspects as percentage of needed income from guaranteed sources, percentage

of guaranteed income used for basic expenses, certainty of achieving portfolio results, etc. Each of these is color-coded green for an acceptable outcome, yellow for an outcome that might need revisiting or tweaking, and red for concerns the system feels needs to be dealt with directly (see Figure 4 on page 22).

360 Pro is intended as a product for a client lifetime relationship, which includes annual updates and reality checks with the client against their planned situation. This lifetime orientation moves the eMoney advisor from a planning position to a lifetime advisor, allowing for future sales, such as in annuity ladders.

The focus of the retirement tools are optimizing income over the projected lifetime of the client, in other words, converting the nest-egg gathered in the accumulation phase into an income stream to last the projected or selected lifetime(s) of the client.

The process begins with the Fact-Finder interview process. If the client had been a planning client previously, the data from that plan is moved over into the distribution phase tool. There are really three levels of retirement income analysis available within the tool; a goals-based needs system, a pure retirement income, and a comprehensive planning solution. Based on the clients' needs and the advisor's compensation, the appropriate level is selected. One output from the interview process is the Risk Tolerance Questionnaire, which is in turn used to select an appropriate asset allocation model.

The asset allocation model is allowed to vary over three distinct time periods, the specifics of which are set by the advisor. These periods are known as "At retirement," "Mid retirement," and "Late retirement." Income streams and expenses can be mapped specifically to these client/advisor-defined periods, or to any other periods that they select.

The system seeks to tie income streams to specific time periods. These income streams are classified as either "guaranteed" where they come from Social Security, pensions or annuities, or they represent liquidation of client asset pools. Social Security is calculated based on benefits available at the selected retirement date. Taxes on additional income are properly matched to Social Security benefit levels. There is no analysis available of the "early benefits and invest model," though a sophisticated planner could incorporate such analysis through changes in the Planning Center.

After income streams are identified, expenses are determined using an elaborate expense panning and budgeting tool. Expenses are also tied to time periods, identified as "basic" or "discretionary," and are inflated at unique inflation rates for each expense. There is a huge menu of possible expenses to assist the client in capturing all their expenditures appropriately. If the advisor feels the client does not have a handle on their future expenditure needs, the advisor can import a "standardized expense hierarchy" summing to a total level of client expenditures. Whatever budget is assembled is then compared to a pie chart of standard expenditure percentages for retirees (Figure 3 on page 21).

Long term care is well handled in the system. It is handled at a high level in the Planning Center, and as a series of alerts (green, yellow, red) throughout the planning process. The exact level of identifying what sets off an alert is based on the configuration set up by the enterprise when they installed 360 or 360 Pro.

Currently, reverse mortgages are not handled in the Retirement Income Tool, however, 360 Pro contains a complete set of reverse mortgage calculations under the “Extra Payments” tab. Payouts from the reverse mortgage can be added as either a lump sum or an annuity, and then fully integrated with the cash flow engine.

One product the eMoney system handles exceptionally well is annuity ladders. Annuities are visited early in the planning process as clients consider whether their sources of “guaranteed income” are sufficient when compared to basic expenses. If there is a poor matching, annuity ladders can be utilized, providing the advisor has the appropriate licenses, to convert some of the asset pool into lifetime income, helping relieve what Evensky calls the “paycheck syndrome.”

Once the plan is completed, it can be stress-tested through a unique series of sliders that look at declining asset values, greater inflation, or changes in tax rates (see Figure 5 on page 23). Monte Carlo simulation is also available, though eMoney indicates that most advisors prefer the sliders as easier for the client to comprehend changes in outside conditions.

Each firm’s setup of 360 or 360 Pro is different, based on what the firm wishes the advisor to consider in terms of report pages, solutions, and products. Firms are provided with Advisor Assurance, a compliance tool that ensures that clients are being provided the correct mix of reporting.

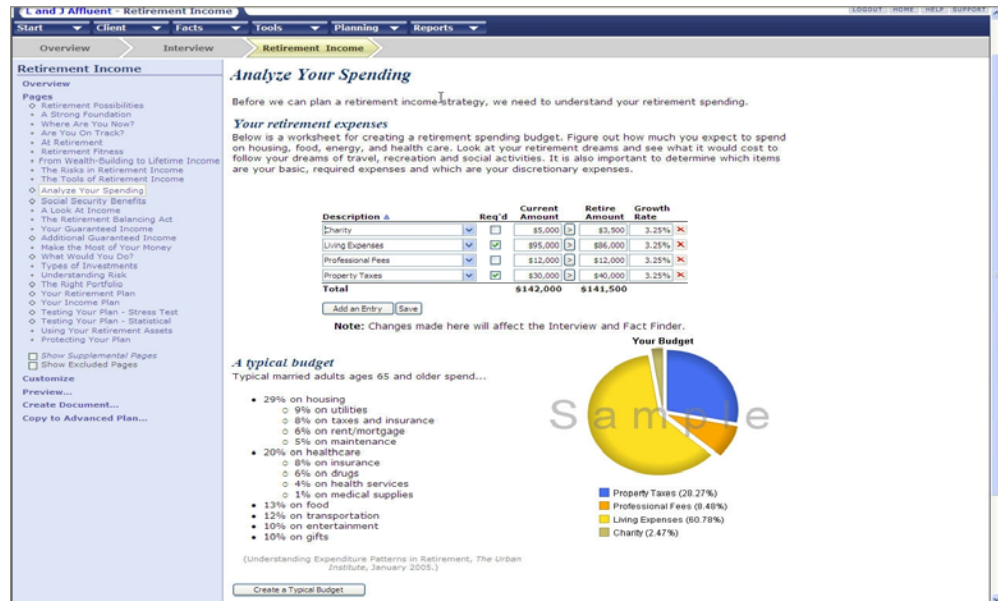
There are no direct feeds from DST, though eMoney has built integrations previously. The system is integrated with CashEdge. Account balances can be pulled in from either Pershing NetXPro or NFS Streetscape. There is no direct integration with trade order management systems, nor are there any automated transaction or asset rebalancing tools. No CRM systems are currently integrated with the eMoney systems.

The entire process can be done collaboratively as both advisor and client look onto the computer. This allows for enhanced, real-time what-if analysis.

The output from the system is a customized, personalized report including all the required pages based on the firm’s requirements, plus whatever the advisor may choose to add.

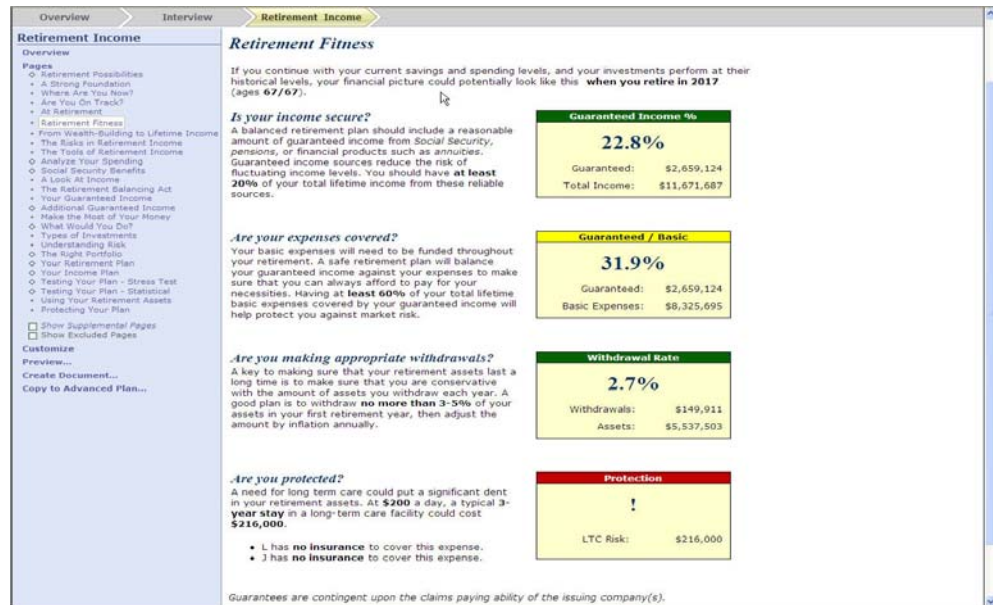
The system is ASP and browser- based, with the client able to access their plan remotely. The system is n-tier, written in .NET 3.5 and utilizes SQL server databases. The system is hosted at SunGard for disaster recovery and back-up purposes. The system is utilized by over 5,000 planning firms, including 18 large organizations such as Mass Mutual, PricewaterhouseCoopers, and MetLife.

Figure 3: eMoney Advisor Spending Analysis



Source: eMoney Advisor

Figure 4: eMoney Advisor Retirement Fitness with Scorecards



Source: eMoney Advisor

Figure 5: eMoney Advisor Stress-Testing Retirement Plan with Sliders

Testing Your Plan - Stress Test

One of the worst things that could happen to a retirement plan is to have a market crash just as you retire. Market losses combined with retirement withdrawals can quickly deplete your retirement assets. Also, an increase in income taxes could cause you to withdraw additional funds from your qualified retirement plans to pay for your expenses.

The Stress Test lets you look at the behavior of your retirement plan in the worst of market conditions.

The Stress Test

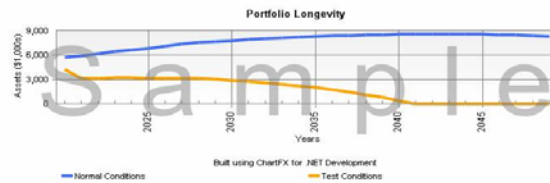
To test your plan, we looked at what would happen if, in most years, inflation and market returns were average, except for years 2020 to 2021, when:



How did your plan do?

During the Stress Test:

- Your assets lasted until age **89/88** in **2042**.
- You were able to fully fund **21 of 29 years** of your retirement.
- You were able to fund **47%** of your basic expenses after your other assets were depleted.



Source: eMoney Advisor

eMoney Advisor Evaluation and ABCD Analysis

eMoney Advisor Evaluation

The following tables evaluate several retirement income and distribution planning factors of eMoney Advisor. The factors were selected based on current evaluations of tools necessary to support the distribution phase and associated income requirements. Table 2 on page 24, Table 3 on page 24, Table 4 on page 24, and Table 5 on page 25 summarize the evaluation of the eMoney Advisor tools.

Table 2: Retirement Income and Distribution Planning Vendors (A)

Vendor & Product	Income from All Sources	Tax Planning	Goals vs. Cash Flow Analysis vs. NPV Analysis	Monte Carlo Simulation	Integration with Accumulation Phase Planning
eMoney Advisor	■ ■	■ ■	Goals and cash flow	■ ■	■ ■

Source: Companies, Celent analysis

Legend: ■ ■ Strong product offering ■ Weaker product offering □ No capabilities

Table 3: Retirement Income & Distribution Planning Vendors (B)

Vendor & Product	Multi-Period Retirement	Alternative Simulations	Long-Term Care Considered	Reverse Mortgages Considered	Target Market
eMoney Advisor	■ ■	■ ■	■ ■	■ ■	Mass affluent and high net worth

Source: Companies, Celent analysis

Legend: ■ ■ Strong Product Offering ■ Weaker Product Offering □ No Capabilities

Table 4: Retirement Income & Distribution Planning Vendors (C)

Vendor & Product	Targeted Advisor Market	Asset Allocation	Integration with Trading Systems	Integration with CRM	Enterprise or ASP
eMoney Advisor	Brokers, insurance agents and planners	■ ■	□	□	ASP

Source: Companies, Celent analysis

Legend: ■ ■ Strong Product Offering ■ Weaker Product Offering □ No Capabilities

Table 5: Retirement Income & Distribution Planning Vendors (D)

Vendor & Product	Budgeting Tools	Expense Categorization	Human Capital Considerations	Partial Retirement Considered	Optimal Social Security Calculators
eMoney Advisor	■ ■	■ ■	■	□	■ ■

Source: Companies, Celent analysis

Legend: ■ ■ Strong Product Offering ■ Weaker Product Offering □ No Capabilities

ABCD Analysis

The ABCD Vendor View shows at a glance the relative position of vendors based on the following categories: Advanced Technology, Breadth of Functionality, Customer Base (number of paying clients), and Depth of Client Services, and is graphically presented in Figure 6 on page 26.

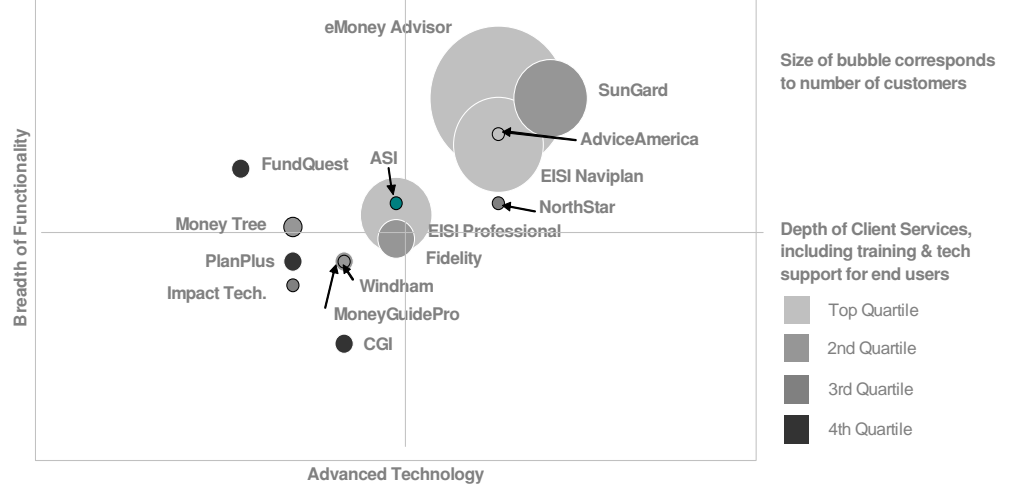
As noted in the Executive Summary, the Retirement Income and Distribution Planning Vendor View has to take into account a large number of systems that do many of the same things, though often in a different manner. It should also be noted that the ABCD analysis is based on current offerings limited to the retirement income and distribution planning space, while future clients may well receive more advanced products currently in development.

In terms of client base, each separate contract with a client was considered as a single client. This means that a contract with a two-person planning shop is equivalent to a relationship with a major firm. Each separate division was also considered as a separate client. Actual counts of planners using the systems, where available, along with specific marquee clients, are included in the text.

For client support, we looked at help desks, training, online tutorials, and best practices conferences. We also looked at business continuity and disaster recovery. For technology, we looked at the difference between technologies that were web-enabled, scalable, utilized modern program languages (as opposed to GUI interfaces on older legacy systems), utilized a variety of database options and had the greatest integration capabilities. We relied on some evaluations from earlier Celent reports in the client report and technology spaces.

Figure 6: Celent ABCD Retirement Income and Distribution Planning Vendor Analysis

Celent ABCD Retirement Income & Distribution Planning Vendor Comparison



Source: Celent

Future Trends in Retirement Income and Distribution Planning

Demographic Trends

- People will live significantly longer, with the average life expectancy of those reaching retirement being in the high 80s or even 90.
- As a result of insufficient savings, the need for income and the desire to stay active, typical retirement-aged people will work longer in part-time positions or in different (but generally lower-paying) jobs.
- Pensions will continue to decline as a retirement income source, even for public-sector employees, meaning people will be even more responsible for their retirement and healthcare costs.
- Social Security will become means-tested, and many high and ultra-high net worth clients will receive no Social Security.
- Medicare will fail or be significantly means-tested and corporate-provided retiree health benefits will shrink or disappear. Both cases will require health insurance to be considered even more in retirement scenarios.
- Healthcare and nursing home care costs will continue to outpace the costs of generalized inflation.

Advisor Trends

- The number of advisors will decline due to retirement and liability issues.
- New advisors will not go into the business at sufficient rates due to liability and sales concerns.
- Advisors will begin to serve, almost exclusively, the high net worth and ultra-high net worth because only those parties will be willing and able to pay for the technology, training, and advice in a fee-based manner.
- Mass market and mass affluent clients will have to rely on self-service and automated solutions.
- Liability cases against advisors and planning firms will skyrocket from retirees who run out of assets in a shorter time frame than predicted by their advisors. Judges will find that financial disclosures in documents, just like those of other products such as pharmaceuticals and tobacco, provide no protection to the advisor, their firm, and other deep pockets who collect part of the fee channel, such as asset managers and custodians. Manda-

tory arbitration clauses will be thrown out in court as result of lawsuits by consumer protection advocates.

Product Trends

- Retirement products will be developed at a faster rate than any other area of retail financial services. The mutual fund companies will lead in development, as their pool of assets are the most likely to run off during the distribution phase. One can also expect that the insurance companies will also be strong product developers around the annuity concept.
- Reverse mortgages will become more common as fees decline and government guarantee regulations allow a greater portion of value to be borrowed.
- Clients will look for “set and forget” products like lifecycle funds and pension replacement products, such as single premium immediate annuities with lifetime annuitization, bond ladders, and annuity ladders, especially in the mass market and mass affluent segments. This will partially be the result of these segments being where advisors will find it less profitable to serve clients.
- Variable annuities will diverge into two types: one featuring expensive and extensive riders and guarantees, and another class of simplified products tied to low-cost indices.
- Long-term care insurance will either mature into a viable planning product or disappear from the investment menu.
- Asset managers, especially mutual fund firms serving the mass market and mass affluent, will continue to create funds to mimic annuities in returning income to the clients, while providing an advantage due to lower fees and less loss of control over the assets.

Retirement Income and Distribution Planning Tool Trends

- Within three years, retirement income and distribution planning will achieve an equivalent level of support by planning technologies compared to the accumulation phase.
- Within 10 years, the retirement income and distribution planning system support will surpass that of basic accumulation planning tools.
- Volatility in markets as a result of the cancellation by the SEC of the “up-tick” rule will become the norm. Monte Carlo simulations will be replaced by alternative simulation methodologies that take into account both histori-

cal and extreme events, which will prove to be more likely and outside a normal distribution.

- Budgeting tools will be required as part of post-accumulation plans. Clients will be required to sign “pledges” that diverting from the budget will have significant negative impact on retirement lifestyles and assets.
- Planning expense systems will have separate inflators for different types of costs, just as they have different return rates for different asset classes.
- Higher mathematics will be incorporated into planning tools to deal with multiple moving parts, such as comparing Social Security benefits at a given date, returns on lesser benefits taken early, switches from full-time to part-time income, and taxes on wages while on Social Security. As of now, no system handles such a complex question that is at the core of every pre-retiree’s situation. It is just a matter of time until such tool is available.

Conclusions

Income after working and the asset distribution phase, following years of sole focus on asset accumulation, are finally getting the attention they need from financial advisors. While the advisor community continues to show less concern about clients in distribution than clients in accumulation, for a variety of reasons, including compensation models, amount of assets, and costs to serve, they can no longer say they lack the tools to properly advise their clients during this key time in their life.

During the distribution phase, mistakes in income can impact the clients' current lifestyle. Mistakes in asset allocation, investment selection, and distribution strategies can have a dire effect on the longevity of the portfolio. Unfortunately for advisors, but fortunately for the clients, the distribution phase for the boomers and subsequent generations will cover a time period as long as their working career, but full of many more pitfalls. Errors in the distribution phase are significantly harder to fix than errors in the accumulation phase, where more savings and different allocations have more time to effect portfolio improvements. It would not be surprising to see more and more lawsuits against advisors for failing to assist clients appropriately in the distribution phase, such as in cases where their assets run out before death.

Slowly, retirement income and planning tools are starting to make their way to the advisors' platforms. As to be expected, those advisors serving the high net worth and ultra-high net worth segments have greater need and financial wherewithal to acquire these tools. This is less true for systems and firms designed to serve the mass affluent and mass market. However, as this report notes, more and more tools are becoming available. As a result, advisors who fail to deploy these tools and utilize them appropriately may be opening themselves up to more fiduciary and legal liability.

Some tools still need to be developed. Better meshing of Social Security calculators and mortality and health tables are needed to help advisors deal with longevity, health, and Social Security benefit risks. These tools will not be simple calculators, but systems that utilize calculus to handle the multiple moving parts, combined with a variety of simulation tools. These tools don't exist today for purchase (perhaps some high-end firms have already developed them for proprietary use by their clients), but are a necessary piece of the distribution puzzle.

Products need to be simplified and made more cost-effective, especially variable annuities, reverse mortgages, and long-term care insurance, before they can enter the mainstream. The costs for these products are too high for clients, and advisors are uncertain as to their responsibility and liability for selling these high-fee products.

Lastly, advisors need to get comfortable with their new roles in this new century. No longer simply planners of cash flows, they are now career counselors, health questioners, and life aspiration coaches. While the sizes of wealthier clients' asset pools support greater training and added specialized staff, this same need is just as significant, if not more so, for the mass market and mass affluent, who really do risk running out of money. These clients cannot be abandoned by advisors as the asset pools decline, as they often have been in the past. Advisors need to develop new compensation models and delivery channels to serve this large population on the edge of their next scary life adventure.