

Top 13 Mistakes Made By Retirement Plan Investors

by Jerry Trask, EA
Suncoast Financial Services

"Only the foolish learn from experience — the wise learn from the experience of others."

Attributed to Romanian folk wisdom by Rolf Hochhuth

Dear Fellow Investor,

Thank you for requesting this free report. I put together this informational piece to help 401(k) and other Retirement Plan investors better manage their retirement savings. Unfortunately, the companies today that administer 401(k) plans have done very little to educate and help plan participants invest successfully; as well as many financial advisors.

Over the next 18 pages I will highlight the most common mistakes I've seen investors make with their 401(k), IRA and pension plans.

Mistake #1: Thinking the 401k is a "free account"

Today's 401k accounts are mainly made up of mutual funds. Unfortunately, most investors have no clue as to how much their 401k costs them.

We first need to learn what the fees are. Mutual fund fees come in four flavors:

- **Annual expense fees** – These can be found in the prospectus. They pay the fund manager, and can vary substantially.
- **12b-1 fees** – Again, these can be found in the prospectus; they pay for the fund's advertising. Generally, they are between .25% and 1% per year.
- **Sales loads** – Simply speaking, these are the commissions paid to the representative for selling you the investment. The most common structures are A, B and C shares. Different share classes will make sense for different circumstances, but they all add costs to your investment. Again, the prospectus is a helpful tool to determine these fees. (Most larger 401k plans do not have sales loads attached to their mutual funds.)
- **Portfolio turnover** – This one is the wild card. Portfolio turnover refers to how much trading is done within the fund throughout the year. The higher the percentage, the higher the costs. Mr. John Bogle's research tells us that conservatively speaking, you pay .5% additional fees per 100% turnover. This may vary from year to year if the fund trades more in some years and less in others.

When you start adding up all the fees, it is not unusual for a fund to cost you more than 2.5% per year. If the markets average 10% per year, then you could easily see 25% or more of your gains eaten away by fund expenses.

Do these expenses show up on your statement? NO! They are taken out of the daily price per share of the mutual fund. As wise investors, we need to know exactly what we are paying, and we must do our best to keep our costs low.

I'll let you figure out how the math works when the market is going down... (Hint: do you think the expenses go away in a down market?)

Mistake #2: Not having a written, proven investment strategy

Successful investors follow a proven strategy and system. Experienced investment advisors call this an “investor policy statement” where you put your goals, dreams, and limitations down in writing. The money is managed according to your long-term objectives and assumptions, not on hot tips or “winging it.” This keeps both sides accountable and removes emotion from the decision-making process.

After dealing with thousands of 401k investors, one thing was shockingly clear to me. Most investors are “winging it” with the largest portions of their retirement! Amazed? Read on. One of the questions I would ask most participants was “How does this 401k account fit into your overall financial strategy?” Are you ready for this? MOST people didn't have an answer. If you are in this camp, please think long and hard about your long-term goals and objectives. The burden of responsibility for employees' retirement has been transferred from employers to employees. This means we all have to make the best possible decisions with our hard-earned savings.

Mistake #3: Not having a systematic formula to determine what type of funds to buy and how much of them to purchase

Many 401k companies today only offer between 5-30 choices for your 401k. Yet it can take as many as 6-10 asset classes and 8-15 investments to properly diversify your portfolio. Many 401k plans don't even offer all of the asset classes we use with our clients as options within their plans.

So out of the 10,000 investment options available, you are working with 5-30 choices. I have found most 401k investors choose the funds in their plan based on past performance, tips from fellow employees, and sales material the record keeper of the 401k sends out. Unfortunately, this ends up in an asset allocation disaster.

Reviewing many retirement plans has given me a keen eye. It's become easy to spot clients with financial planners because it is obvious when looking at their investments. As a guess, less than 5% of the 1,000 or more accounts I saw had what I would consider a good mixture of investments. The company that handles your 401k is getting paid based on the fees they charge your employer AND the annual expenses paid by

participants like yourself. Basically, they are making lots of money whether you succeed or fail. If you are still an active employee, don't expect much help from the firm that handles your firm 401k. They will probably not even contact you until you retire or change jobs, BECAUSE IT IS AT THAT POINT YOU CAN FIRE THEM!

Mistake #4: Investing while looking in the rear view mirror (Investing in HOT FUNDS that have been making lots of \$\$\$\$\$\$)

If you learn nothing else from this report, PLEASE do not invest your portfolio in the "hot funds." Although hot funds are those which have done well in the most recent time frames (think Technology in 1999/2000), this is by far the easiest way to lose money in the market. Dalbar reports that from 1982 to 2002, a period when the market averaged over 12.75%, the average investor only earned 3.5%. That is like paying an 8% load EVERY SINGLE YEAR! Why? Because investors buy high, sell low, chase returns, and invest in expensive products with high annual expenses.

Investors lose money by extrapolating some previous trend too far into the future. Here are a few painful lessons some investors have learned the hard way:

1980	Commodity, Precious Metal and Oil Craze
1990	Japan Craze
1998-1999	Index Fund Craze
1999	Large Cap Craze
1999-2000	Technology, IPO, and garbage.com Craze
2000-2005	Real Estate Craze along the East and West Coast
2006-2008	China, Russia, Brazil, India, etc.
2008-2011	Gold, Silver, Commodities and Oil

Want a good investment idea? AVOID every super-popular investment you find. This will keep your portfolio intact for the long term. Develop a strategy and stick with it.

Mistake #5: Overlapping investments

Ever wonder why you own 5 mutual funds, but your account either stays flat or goes down? One reason could be your investments are too correlated to one another. This means you can own 4-5 mutual funds, but the funds could be investing in the very same stocks. One great example is Fidelity Magellan and the S&P 500 index fund. Did you

know that over the past few years they were 98% the same – only Magellan was three times as expensive? If you held both funds, you received basically NO diversification. The point behind asset allocation is that by spreading the money in your portfolio around (we call it reducing standard deviation or variability of returns), some areas do well when others don't.

We have special software and tools which allow us to gauge the overlap of investments inside your account. Therefore we can make sure you are not doubling up on exposure to certain areas of the market. Often we will hear people complain about losing money with their investments. Unfortunately, these people treat investing like a game, and do not take advantage of the time-tested techniques of preserving and protecting their wealth.

Mistake #6: Lack of professional support

Have you had a professional financial planner review your retirement plan in the past 2-3 years? Brokers who “glance” from time to time but never provide any written analysis may not be doing what you think they are. Many “financial advisor” types only want to help you before you become a client. Once the sale is done...it's “NEXT” to another prospect.

I would encourage you to work with a CERTIFIED PUBLIC ACCOUNTANT OR CHARTERED FINANCIAL ANALYST™ who can help review your investments and provide advice – regardless if you are retired or still active with your employer.

At my firm we have 2 options for our clients. One is a retirement check up where you pay a flat fee for a portfolio review. The other is letting us manage your account for a fee or percentage of assets per year. The choice is yours. By the way, steer clear of “advisors” who act like salespeople and pitch loaded funds, B shares, or annuities. In many instances they are doing so either because they want to maximize their commissions or they can't charge you annual fees to manage your accounts. Know exactly what you are getting yourself into!

Mistake #7: Asset allocation Train Wreck for 401k plans

Have you ever wondered how really smart people invest their millions and billions of dollars? Harvard and Yale have both produced some of the smartest investment minds in the industry. Today their alumni often run mutual funds, hedge funds, and private endowments. They sit on institutional boards and run some of the largest investment firms in the US. Basically, they are the “Who's Who” of the investment world.

You might not know this, but Harvard and Yale are very well known in the investment world for having the most successful endowments today. They have flat out been CRUSHING their peers. This chapter is meant to illustrate how they invest their private

endowments (otherwise known as their private stash of cash) and compare that to how many individual investors handle their 401k accounts.

Harvard's Asset Allocation	vs.	Most 401k Investors.
15% US Stocks		100% money market
10% Foreign Stocks		or
5% Emerging Markets		3 Domestic Stock funds
13% Private Equity*		or
12% Absolute Return*		50% company stock
5% High Yield		50% US stock funds
13 % Commodities		or
10% Real Estate		4 Overlapping funds
11% Domestic Bonds		or
5% Foreign Bonds		a Variation of Above!
6% Inflation Protected Bonds		
-5% Cash (to spend)		

*Might not be available to individual investors

Notice the difference here? Harvard calls their investments “a well-diversified portfolio with an attractive risk-return ratio.” What do you think they would call most 401k accounts today? I bet they say they’re a train wreck waiting to happen. Notice how Harvard spreads their billions around nine different asset classes. Their endowment feels this mixture helps to increase their return while reducing risk!

Not a fan of Harvard? Here is what Mr. Jim Swenson, the manager and person who runs Yale’s endowment said:

“Currently at Yale, we’ve got a half dozen asset classes that individuals ought to have in their portfolios. Traditional bonds, inflation-indexed bonds, US Stocks, foreign developed stocks, emerging market equities, and real estate securities.” He then argues we should limit ourselves to 30% in US stocks.

He went on: “The problem with the mutual fund industry is that you’ve got a sophisticated provider of investment services on one hand, and, on the other, you have an unsophisticated consumer. That imbalance leads to behavior that lines the pockets of mutual-fund managers at the expense of the individual investor.”

How does your portfolio compare to what these two fine educational institutions are doing with their own money?

By the way, if you have a professional advisor, he/she could be abusing you as well.

Most advisors are trained as salespeople and not as planners or investment experts. I would be willing to bet we are the FIRST people to show you the Harvard and Yale philosophies. Yet many trust departments at banks implement these types of strategies

with their client accounts. It's not fair that only people with \$25 million dollar accounts at bank trust departments get to implement these strategies!

Mistake #8: Moving your 401k to a salesperson and not a trusted fee-based advisor

Let's assume you wanted to delegate your portfolio to a trusted financial advisor. What should you look for? Here is what I would consider, based on my seven years in the industry:

- Someone who has already been in the industry between 5-10 years and will continue to be in the industry for a while.
- Someone who has designations after their name. CPA, CFA, CFP
- Someone who works on a fee-basis rather than as a salesperson (loaded funds, expensive annuities or B shares.)
- Someone who takes time to review your big picture.
- Someone you trust.
- Someone who has an open architecture (no "product lists.") Many banks and insurance firms have small product lists for their advisors to choose from. JUST SAY NO! (Advisors call this their approved list.)
- Someone who is going to work with you in the future (quarterly and semi-annual reviews.)
- Someone with an educational background in business & investing (CPA, finance degree, MBA or both.)
- Someone who is associated with a boutique/specialty firm (I consider independent advisory firms my stiffest competition.) Happy clients rarely leave them.
- Someone who takes a planning-based not a product-based approach.
- Someone who will prepare a comprehensive financial plan rather than just focusing on investments.

Mistake #9: Staying in your 401k when you have the option of moving to an IRA

In the next section of this report, we'll go into great detail as to why individuals should consider moving their 401k/Pension account to IRA accounts instead of leaving them in their employer-based plan. To summarize, here are a few of the reasons:

- Professional help
- Greater withdrawal options
- Much wider range of investment options
- Access to asset classes/institutional shares not offered in 401k plans
- Beneficiary options after death
- Special tax treatments of highly appreciated company stock

- Access to after-tax money to use for spending
- Breakaway from restrictions the company placed on withdrawals or exchanges
- Elimination of some of the fees 401k plans can charge
- Avoidance of 401K plan destruction to your estate planning (401k plans often kill bypass trusts a/k/a AB trusts)

Mistake #10: Thinking someone at your company is “watching over your account”

401k accounts are self-directed. What that means is that YOU are ultimately responsible for making EVERY decision regarding the welfare, maintenance, and performance of the account. Some retirees who have worked for their employer 25+ years often have the misunderstanding the company has “done what is right by them.” This varies based on the company.

The important thing to understand is that your 401k is like an account you would hold at a discount broker. EVERY decision is up to you. In today’s competitive global marketplace, companies are more concerned about making money than the welfare of your retirement account. You need to act accordingly.

Mistake #11: Investing in high commission-based investments

There is a huge difference between an investment advisor and a “broker.” Investment advisors are fiduciaries who are legally responsible to act in your best interest. “Brokers” might make more in commissions in 5 minutes on your account than a trusted advisor might make in 6-7 YEARS. Therefore the sales pitch is going to sound nice and juicy.

Unfortunately, many large banks, investment firms, and “brokers” want only one thing.

Their goal is to generate the highest revenue with the least amount of effort and money possible. This might not even be the broker’s fault. Many friends have worked as a “registered rep” for a major Wall Street Investment firm. Many of the “brokers” for the firm sold the highest commission-based products because the bank or investment firm had structured their pay plan in such a way that they sometimes kept 80% of the revenue.

Here are the some of the highest commission products “brokers” might try to pitch you:

- 1. Equity Indexed Annuities** – Commissions up to 10-12% of the amount invested (You invest \$250,000 and that firm gets a \$25,000 payday!)
- 2. Loaded Mutual funds** – Usually 5% up front of backend fees. Loaded funds are not all bad, but the advice you get AFTER THE PURCHASE is going to vary a lot. What incentive does a “broker” have to work with you if they already have made their money?

If you do purchase loaded funds, make sure your broker is using breakpoints to lower your overall fees.

3. High Expense Mutual funds – There are funds out there that have annual expenses over 2%. Add in trading costs and you might be doomed before you even begin (2.5% on \$250,000 is \$6,250 PER YEAR.)

4. Expensive Fee-based Advice – Add up ALL of the fees. You might have to pay your broker, your broker’s firm, investment managers, and trading costs. The higher the total number, the harder it will be for your portfolio to survive.

5. Variable Annuities Loaded with Guarantees – Insurance companies have gotten very creative. You can now buy all type of guarantees with annuities. However, the devil is always in the details. Read the fine print! These annuities pay 6-9% upfront commissions, so keep that in mind. Be skeptical.

Here is what a former SEC Chairman has to say on the issue:

“You should fire your broker and find an investment advisor. Brokerage firms would like you to think that they perform the same functions as investment advisors. Many brokers call themselves ‘financial consultants’ or ‘financial advisors’. But they are not the same as independent investment advisors... an investment advisor’s fiduciary duty is on a higher plane, like that of a lawyer, a trustee, or the executor of an estate.” - Arthur Levitt, Former SEC Chairman

Mistake #12: Not learning from the history of the market.

Market Cycle		#		PE RATIO		INFLATION		DOW JONES	
From	To	Total Years	Market	BEG	END	BEG	END	BEG	END
1901	1920	20	BEAR	23	5	-2%	16%	71	72
1921	1928	8	BULL	5	22	-11%	-2%	72	300
1929	1932	4	BEAR	28	8	0	-10%	300	60
1933	1936	4	BULL	11	19	-5%	1%	60	180
1937	1941	5	BEAR	19	12	4%	5%	180	111
1942	1965	24	BULL	9	23	11%	2%	111	969
1966	1981	16	BEAR	21	9	3%	10%	969	875
1982	2000	18	BULL	7	42	6%	2%	875	11497
2000	????	?	BEAR	42	?	3%	?	11497	??

Source: Crestmont Research

<http://www.crestmontresearch.com/pdfs/Stock%20Secular%20Annotation.pdf>

One of my personal passions is studying the history of the stock market and the economy in general. My fascination began in 2000 watching the NASDAQ crater. I became intrigued with the market fallout, especially how Wall Street could have been so wrong.

If you remember, Wall Street was pumping up the biggest stock market bubble of all time – reinforcing our beliefs that the stock market “always goes up” and that we were in a “new economy.” “It is different this time.”

The chart above is one of the very best educational pieces I have ever seen.

What I want you to learn from this chart is the following:

The stock market has a history of going from Cheap to Expensive and back again over long periods of time.

The larger the bull market, the longer the bear market that follows it.

Inflation historically rises from low points to higher points during bear market periods.

The stock market historically does well during periods of falling interest rates and falling inflation.

What does this mean for the future?

Investors need to prepare themselves for the fact the US stock market (as a whole) might stay flat or “muddle through” for several years to come. Inflation during this period historically rises.

You want to invest some of your portfolio in assets that do well during times of rising interest rates, higher levels of inflation, and a flat stock market.

To sum up, the flat market we have experienced since 2000 is perfectly normal and might continue for some time to come. This is one reason I love the Harvard Endowment approach for the upcoming 5-10 years. This approach should help diversify your portfolio, thus hopefully giving you a higher return with less risk.

Most 401k plans are not set up to do well during secular bear periods because most 401k plans lack the investments that do well during these periods!.

Hint: Historically, commodities are the place to be when the market goes sideways. Rising commodity prices are usually bad for corporate earnings.

Authors have written 400-page books on this subject.

WARNING: Most financial people who would give you advice either do not study market history or were not in the investment business during the 1970s.

Mistake #13: Not exploring the alternatives available for inexpensive and effective diversified investing

To answer this question, we need to have a good understanding of what diversification means and how we benefit. Then we can discuss the particulars.

The bottom line goal of diversification is simple: higher average returns with less risk. Simple goal, but not so simple to accomplish!

As you can imagine, this has been the Holy Grail of investing ever since investing began. Wouldn't it be great to capture high returns with little or no risk?

Obviously we haven't solved this one yet. Investing and risk still go hand in hand. But we have made some headway over the years in understanding risk and learning how to minimize it to some degree.

Reader Beware: We are about to briefly (I promise!) enter the world of academic studies, so take a deep breath...and away we go!

Much of our current learning comes from something known as "Modern Portfolio Theory." This began with Harry Markowitz's research in the 1950s which actually led to his winning the Nobel Prize in 1990.

Without going into all the details (I'd like you to stay awake!), Harry learned that because different investments behave differently, we can mathematically determine portfolio mixes that will have a high likelihood of lowering overall risk, while at the same time providing the highest probable returns. He called it the "Efficient Portfolio."

A famous study was then conducted by Brinson, Singer, Beebower called: "Determinants of Portfolio Performance II: An Update," published in Financial Analysts Journal in May-June 1991. In many regards, it was a test of Markowitz's Modern Portfolio Theory – and it proved Harry was right. Here's what they learned:

Over time, returns earned by a portfolio are determined by the four following factors:

Asset Allocation (Markowitz):	91.5%
Manager Performance (good or bad):	4.6%
Fees / Expenses:	2.1%
Market Timing:	1.8%

What does this all mean? It means that how you **structure your asset allocation** has by far more impact on your investment returns than anything else!

So what benefit does diversification bring us? This is the part most people miss! Proper diversification lowers risk, which means less volatility.

And lower volatility is better for you!

Here's a simple example to illustrate the point:

(Note: This is a hypothetical example and does not represent any specific investment.)

Portfolio A has the following annual returns:

+40%, -20%, +10%

Portfolio B has the following annual returns:

+10%, +10%, +10%

Notice that both Portfolio A and B have the same 3-year average return of +10%. But assuming we start with \$100,000, here's what happens:

Portfolio	Value	Year 1	Year 2	Year 3
A	\$100,000	\$140,000	\$112,000	\$123,200
B	\$100,000	\$110,000	\$121,000	\$133,100

Over time, lower volatility can create HUGE differences in portfolio values!

OK, academic discussion over. Pat yourself on the back for staying with me!

Again, what does this new understanding of volatility mean to you?

For some, it could be the difference between continuing their membership at the country club or not.

For others, it could be the difference between going on vacation with the grandchildren or not.

And for many, it could mean the difference between worrying about (or even having to) go back to work instead of enjoying a carefree retirement.

The bottom line is this – retirement is the time in your life when you should be able to count on more consistent returns on your money. This is the time when you can least afford volatility as it can severely impact your Golden Years.

Now that we have the basics (believe me, we just touched the surface), we can look into mutual funds and alternatives (ETF's).

Right away, if you have been paying attention, you are probably thinking you can simply determine your appropriate asset allocation and go invest in a group of index mutual funds.

I would tell you that yes; you would almost certainly be improving your circumstances by taking this approach.

But I will also tell you that you are acting on only partial information!

Diversifying across asset classes is important, but by no means have we completed the diversification puzzle. This is just the first step on the road of lowering volatility (however, further discussion will quickly go beyond the scope of this report.)

So how do we accomplish diversification inexpensively without using regular load or 12b-1 mutual funds? We employ a combination of four alternatives to build a fully diversified portfolio.

They include:

Regular Mutual Funds
Exchange Traded Funds (ETFs)
Separately Managed Accounts (SMAs)
Institutional Mutual Funds

Given the four alternatives listed above, you can build a completely diversified portfolio WITHOUT many of the problems encountered in the retail mutual fund industry. (Please remember the above alternatives do contain market risk and are NOT FDIC insured. As they also have different expense characteristics, you will want to review a prospectus prior to investing.)

So where do you go from here?

By now, if you are like most people, you are wondering:

Are my mutual fund/investment holdings any good?

and

Would I be better off doing something different?

To help you obtain clarity in this complicated area of planning, we will provide you a **FREE EVALUATION** of your investments.

For your **FREE INVESTMENT EVALUATION**, you need only to take the following simple steps:

1. Call our office at 727-612-0495 to schedule a complimentary meeting (no sales pitch, we promise!).

2. Complete the Confidential Financial Profile we will send you.
3. Bring the profile to your meeting, and we will evaluate your current funds for absolutely no cost whatsoever.

If you choose, we can discuss our services. If not, the analysis is yours to keep for FREE.

This FREE analysis will uncover the following useful and important information on your mutual funds:

- Analysis of the true total expenses charged each year on your funds, whether held individually or in a variable annuity
- Manager performance analysis to determine if your fund manager is doing worse or better than comparative benchmarks
- Tax analysis to help you better understand the tax consequences of each mutual fund holding
- Portfolio analysis to help you learn what your current asset allocation REALLY looks like and if you can lower your risk, yet have the same or better expected returns over time
- General thoughts on your current holdings based on our limited knowledge of your circumstances

A couple of promises:

**We guarantee complete and total privacy of your information
We are NOT going to be calling you trying to sell you something!**

How do you know that we know what we're doing?

That's the thousand-dollar question, isn't it?

The best way you can evaluate investment advisors to determine their capability is to look at their credentials and licenses. In the investment advisory world, there are a number of well-known credentials and licenses that are helpful to ask about:

- Are you a Registered Investment Advisor (RIA)? Many financial advisors are not. RIA firms are fiduciaries that must represent the client and recommend to the client only what the courts consider prudent. The two regulatory agencies that license RIAs are the Securities and Exchange Commission (SEC) and the State's Department of Finance and Securities.
- Are you a CPA or CFA or CFP®? Many financial advisors are not. Initial course study encompasses a minimum of one year of preparation and a lengthy exam process. They must also comply with strict ethics, and complete hours of continuing education every year.
- Are you a Registered Representative with a NASD member firm and have a Series 7 registration (a six-hour exam)? Many financial advisors only have a Series 6 registration (or none at all), limiting their product availability to solve their

clients' needs. Registered Representatives are licensed through member firms which are regulated by the National Association of Securities Dealers (NASD). Most of these professionals "sell" products.

So why do I do this?

Why do I go through all this effort for free?

Simple – I know that when you order your FREE INVESTMENT ANALYSIS, some of you will take the information I provide and implement it yourself. And that's OK!

But some of you will take the information and say to yourselves, "This analysis is terrific! This might be the kind of financial advisor I need to help me with my planning. I want to talk to this guy to learn more!"

And you know what? A certain number of those folks will decide they like me and that I would be a good fit for them. But presently in order to maintain a high level of service to our existing clients, we accept only a limited number of new clients each year and require a minimum investment of \$50,000.

That means that even if you think we would be a good fit for you, we have to determine if you are a good fit for us.

So for those folks who want to talk to us further, we have a number of meetings to ensure a relationship will be good for both of us.

It's a win/win for all of us – all of you get a free analysis, some will find the financial advisor they have been searching for, and I will end up with a few select new clients for the year.

So go ahead, fill out the FREE Evaluation Form and send it to us in the enclosed envelope. You will receive your FREE ANALYSIS within 2 weeks of sending forms in.

Warm Regards,

Jerry Trask, EA

P.S. Don't forget that you have nothing to lose!

P.P.S. Check out our website at www.taxprep911.com for upcoming events and great information!

P.P.P.S. Everything is 100% confidential! Your privacy is completely protected!