

# **Testimony for Department of Labor ERISA Advisory Council on Financial Literacy**

**By Liz Davidson, Founder and CEO of Financial Finesse  
September 19, 2007**

## **1. Does the plan sponsor have any responsibility to educate the participants about their decisions at retirement?**

Absolutely! Any firm that offers a retirement plan should provide employees with financial education around how to make informed decisions on how to use these plans to achieve their retirement goals. This is particularly true for firms that have recently terminated their Defined Benefits Plans or firms that have auto enrollment at a low deferral rate. The risk in both cases is that employees assume they are set for retirement, only to have a rude awakening when it is time to retire.

In terms of decisions those ready to retire are facing, this is critical as well. We've found that most employees are woefully ignorant about their retirement distribution options and the tax consequences as well as pros and cons of each. Those who are retiring early are often unaware of penalties involved in early withdrawal.

In addition to having a moral obligation to educate employees about retirement, it is in the company's best interest to provide broad-based financial education programs to their employees. These programs have helped employers increase pay satisfaction, reduce turnover, increase productivity, increase retirement plan participation, improve asset allocation within the retirement plans, and help employers to pass retirement plan discrimination testing.

## **2. Are programs in place now adequate for sound decision making? Why or why not?**

Most programs are not adequate for sound decision making for the following reasons:

1. They are provided by financial services salespeople who have a vested interest in commissions associated with selling investments and are not trained as financial educators.
2. They are limited to asset allocation and choosing investments and do not address the biggest barrier to retirement planning which is saving enough. Basic money management skills are rarely a part of retirement planning education and they are perhaps the most important piece of the puzzle.
3. They are launched as one time events or annual events, rather than an ongoing process—studies show people need to hear a message 7 times before they remember it and act upon it.

4. They are often delivered in lecture or talking head PowerPoint format, which is the least effective way to educate people. Studies show this form of education has only a 5% retention rate. The retention rate jumps to 70% when you create interactive education where participants are actively involved in their own learning.

**3. Should the plan sponsor receive any incentives to provide this education? What would be a sufficient incentive?**

I believe a tax credit should be offered. It can be done on a per employee per year basis and can be as little as \$5-10 per employee per year for larger companies; more for smaller firms to cover the costs required to educate.

At the very least, an employer could be certified by DOL for having provided the education and could use this certification to recruit employees and help qualify for HR awards and accolades, such as Best Company to Work For.

**4. What specific message should participants receive at retirement? What are the preferred ways to deliver the message?**

Specific Messages:

How to effectively manage retirement assets, in terms of distribution, continued investment and budgeting to ensure they don't outlive their assets. This is the most important message of all.

How to set up necessary estate plans to ensure the assets are distributed the way they want when they pass away. This is relevant to anyone who wants to leave a legacy as opposed to spending down most or all of their assets in retirement. We've found that most people would prefer to leave assets to loved ones.

How to make critical health care decisions related to: retiree medical plans the company may have in place, Medicare and Medicaid, private health insurance, long term care insurance, and effectively budgeting for both premiums and out of pocket health care expenses.

Preferred delivery methods:

One-on-one is best and ideally also face-to-face. Otherwise, phone-based financial coaching is also an acceptable delivery method. Financial Planning calculators should be provided as a follow up, so retirees can calculate the effect of different distribution strategies on their future income.

In companies where this isn't viable, workshops should be done for all employees within a year of retirement and opened up to retirees who want to attend as well.

**5. In addition to management of retirement savings, what are the three main financial issues facing retirees? Are there regulatory hurdles? If so, what do you recommend to aid retirees without undue cost and burden to the employer?**

3 Main Financial Issues

Health care: Knowledge of Medicare and Medicaid, choices associated with retiree health plans, private insurance, long-term care, and correct budgeting of health care expenses.

Estate planning: Creating wills and trusts, updating beneficiaries, and sheltering assets from future estate taxes.

Preventing Fraud: This is a bigger issue as retirees get older due to the fact there is a high incidence of dementia and Alzheimer's and also loneliness/isolation issues due to losing a spouse. This can increase their susceptibility to being taken advantage of.

Recommendations on how to aid Retirees with these decisions:

Personal Financial Consultations in person.

Retirement Security Workshops.

Financial Support as needed over the Phone (Excellent for fraud protection).

**6. What potential disruptions to retirement income stability exist for retirees?**

Potential disruptions include: Living longer than expected, health care costs being higher than expected, financial planning fraud and/or inappropriate investments sold to retirees, significant market declines, and poor budgeting/expense management.

**7. Inherent within "advice" provided to participants is the specter of fiduciary responsibility. Can "education" be provided without fiduciary responsibility and still deliver effective information for retirement decision-making regarding personal finances and health care?**

Absolutely! On studies of participants in our education programs, on average approximately 80% report that they have taken significant actions to improve their financial situation to improve their financial situation. The number is highest for employees that attend multiple workshops and/or supplement workshops with Personal Financial Coaching and it is higher for those that have Defined Contribution Plans as their sole retirement vehicle versus those that are covered by a Defined Benefit Plan. It is also marginally higher among pre-retirees, though the difference between pre-retirees and those further from retirement is not that significant (less than 5% differential based on early hard data as well as anecdotal data).

**8. Should the prohibited transaction exemption provided for investment advice contained within the Pension Protection Act of 2006 be expanded to allow for other forms of financial advice, e.g. insurance, health care choices? If so, what safeguards would you recommend for satisfactory regulatory oversight of such and expanded PTE?**

I would recommend that there be some standards to ensure that the program is educational rather than sales oriented in nature. The biggest risk is that the PTE actually harms employees by opening the door to financial services salespeople to recommend highly lucrative but not necessarily appropriate investments for employees. Without safeguards, there is much greater potential for fraud.

I would recommend the following safeguards:

1. The government should develop best practice guidelines as to how companies should choose firms to provide financial education. These would include guidelines on reviewing track record and experience in providing financial education to similar companies, results of their education programs, comprehensiveness of their curriculum, safeguards the provider has in place to protect against conflicts of interest, and training and experience of planners providing the education, among other things.
2. The government should have a program in place to review financial education companies and financial services firms in order to validate that they are following all the safeguards and the DOL should officially certify firms that do follow the safeguards.
3. The education must be unbiased in nature—ideally provided by a firm that does not sell financial products or services and therefore has no conflict of interest. If it is delivered by a financial services company, no commissions can be made off the sale of financial services. If an employee wants to work with the financial services provider after the workshop, all charges must be hourly or based on fees for the actual financial plan, not the financial products.
4. The financial services provider must provide a record to the employer of all fee based revenue generated from the education on a quarterly basis and must certify that all sales were initiated by employees of the plan sponsor, not a representative from a financial services firm. Under no circumstances should the financial services provider be allowed to solicit employees.
5. The plan sponsor should have a separate, independent education effort in place to ensure that employees have an understanding of how to select and manage a financial planner and a basic education on financial planning principles so that they are less likely to fall victim to fraud.