Understanding Errors in Retirement Planning

August 3, 2022 by Dr. Harold Wong

Over the decades, millions of Americans have made major errors in their investment, tax, and retirement planning decisions by not understanding advanced math. I will cover two examples now, including common myths.

Mistake #1: I can average 10-12% rates of return in the stock market!
If one examines academic studies, a better mathematical measuring stick would be Compound Average Growth Rate (CAGR). MoneyChimp.com calculates that the CAGR was 5.49% from January 1, 2000 to December 31, 2022. Why is this about half of the return that many Americans believe they can earn in the stock market? This example will illustrate.

Suppose you ended the Dot-Com Boom with $1 million in the stock market on 1/1/2000. Then the Dot-Com Bust started and on 1/1/2001, you are down by half to $500,000, which is -50%. You got lucky in 2022 with some stocks that had big gains and now have $900,000 on 1/1/2022, which is +80%. The algebraic total is +30% and so your average return is 15% for the 2 years, even though you are down $100,000. At this point the seminar audience is stunned and confused. If folks really understood advanced math, they might not have 80-90% of their life savings in the stock market.

Myth #2: Making Big Returns in the stock market is more important than saving taxes!
Example: an engineer and his spouse are both age 70 have $3 million of financial assets, of which $1 million is in an IRA. They think they can average 10% annual returns in the stock market forever and we assume they will be that lucky. Both have old-fashioned pensions and have maximized their Social Security by waiting until age 70 to start it. Their normal taxable income is $200,000 before pulling money from their IRA. They both have family histories with long life and expect to live until age 95. Their combined federal/state tax bracket is 40%. They have 2 kids.

If they earn $100,000/year in their IRA and pull it out, they will owe $40,000/year in taxes. If they could convert the $1 million IRA to a Roth IRA, they could save $40,000/year. Let's now go to an advanced concept: economic opportunity/cost benefit analysis, which I have not seen in any of the hundreds of financial seminars I've attended over the last 50 years. I was not exposed to this concept until taking Ph.D Economics courses at UC Berkeley.

Using a financial calculator, enter: $40,000/year for annual payment; 10% for expected annual return; 35 years for time; and click FV for Future Value. The answer is $11,925,072 more net wealth is created for the family by the Roth IRA. The reason we use 35 years is because when a Roth IRA is inherited, the kids can earn unlimited amounts for the first 10 years and adds to their 25 years from 70 to 95. If one could save $40,000/year taxes for 35 years, that's $1.4 million total. However, one would not account for the fact that adding $40,000/-year to your investment money machine means almost $12 million more wealth.

Note: if one only has $400,000 in an IRA, converting this would create $4,777,028 more net wealth for the family. You don't need to increase risky investments; just save tax to create a great family future! Please attend one of my future seminars to find out how to do Roth IRA conversions without paying any federal income tax.

Free Live Seminar and Lunch: Saturday 9/24/2022 at Hyatt Place, 3535 W. Chandler Blvd. Chandler, AZ 85226, with seminar starting at 10 am and Free Catered Lunch at 12:15 pm. Topic is "Beat Inflation by Saving Lots of Tax and Increasing Cash Flow!"
To RSVP for the seminar or schedule a free consultation, please contact Dr. Harold Wong at (480) 706-0177 or harold_wong@hotmail.com.

Free Information on Retirement Planning, Solar Business Investments, and Tax Savings can be found at www.drharoldwong.com or www.solarbusinessinvestments.com.

To schedule your Free Consultation Contact Dr. Harold Wong at (480) 706-0177 or harold_wong@hotmail.com to RSVP.

Dr. Harold Wong earned his Ph.D. in Economics at the University of California/Berkeley and has appeared on over 400 TV/Radio programs.