401(k)aos

HOW OUR DREAM OF RETIREMENT BECAME A NIGHTMARE OF CHAOS

A Shocking Look at Wall Street's Greed and Deception and How You Can Win the Battle to Restore Your Dream of Abundance in Retirement

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FOREWORD BY ROBERT KIYOSAKI

Dedication

To Robert and Kim Kiyosaki
for encouraging me to share what I know.

Acknowledgments

I want to acknowledge my friend and business partner Mike Denison. My English teachers told me I would never amount to much, let alone write a book. Without you, Mike, they would have probably been right.

I would also like to acknowledge Mona Gambetta for her invaluable contribution to the creation of this book. Her expertise has helped bring this information to the public so everyone can benefit from these vital insights.

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Foreword
by Robert Kiyosaki

401(k)aos: Not for Everyone

In 1994, my wife Kim and I retired. We were financially free. Kim was 37 and I was 47. We still had our lives ahead of us—and we were free from the drudgery of going to work to earn a living.

We achieved our freedom without traditional jobs and without a 401(k), the retirement program millions of people are counting on.

There were many reasons why we did not have a 401(k) and Andy covers most of them in this book. And this is why this book is so important—especially for people who *have* a 401(k).

The primary reason we did not have a 401(k) is because we did not need one. Having had a rich dad in my life, I had the financial education to manage my own money. I did not need someone else to do it for me.

The secondary reason was because Kim and I could do better, as investors, by *not* investing in the 401(k) program. Our returns on investments were far greater, faster, and much less risky than traditional investments.

The third reason was because we did not trust the 401(k) program. It did not make sense, was complicated and confusing...and too risky for us.

That being said, this does not mean that a 401(k) is not right for you. For you, a 401(k) might be your best bet.

The reason this book by my friend and Rich Dad Advisor Andy Tanner is important is because it allows you to see the good, the bad, and the ugly of the 401(k) program. Then you can decide if it is good or bad for you.

Obviously, if you decide as Kim and I did, that the 401(k) program is not for you, the next question is "What is right for you?"

That is the most important question of all.

Good luck,

Robert Kiyosaki,
Investor, Educator and Author of
Rich Dad Poor Dad and the *Rich Dad Series*

Introduction

This book is about you. It's about your life, your dreams, and your future. It's about why we entrust our financial security to those in authority. Most importantly, it is about how that trust has been betrayed in monumental ways that are only now starting to become apparent to the millions who have invested in these retirement vehicles.

We live in an amazing country that is both vast and diverse. Despite all of our differences, it's interesting that nearly everyone has one thing in common: a 401(k) account provided by our employers.

With the massive number of 401(k) retirement accounts in the United States, it's easy to see that this really is one of the ties that binds us together.

In the Internal Revenue Code, which is the taxation rule book in the United States, sub-section 401(k) defines a type of retirement plan funded primarily by an employee to build for one's own retirement. The 401(k) plan is a relatively new investment vehicle, having arrived on the scene as recently as 1978. The first wave of retirees banking on this vehicle as their ticket to the retirement of their dreams have yet to test its worthiness and its ability to deliver on the promises made under its guise.

I'm here to tell you: The day of reckoning has arrived.

We have been promised many things from these 401(k) plans: big gains through the stock market, matching funds from employers, professional management, tax deferrals, and more. Now that these plans have a track record of real-world results, it's a good time to look at whether or not the average person is benefitting from these retirement programs and how all of the big promises are playing out.

Throughout this book we will discuss the specific 'promises' that are part of the 401(k) sales pitch—and expose them as the dangerous lies they are. Lies that are causing serious harm to millions of unsuspecting victims. As a result of these lies, it will be difficult if not impossible for the vast majority of people who have 401(k) plans to have enough money to retire with the standard of living they had always envisioned. Their reality will, most probably, be very different from anything they ever imagined.

Although 401(k) plans are an American creation, the concept is spreading like wildfire around the world. If you live outside the United States, you probably have a 401(k)-type plan available in your country. You'll find they're referred to by different names, such as:

- Australia – Superannuation System
- Canada – Registered Retirement Savings Plan
- France – Special Retirement Plan
- Mexico – Retirement Funds Administrators
- New Zealand – KiwiSaver System
- Singapore – Central Provident Fund
- United Kingdom – Pension Provision
- Germany – Betriebliche Altersversorgung

For simplicity, we will refer to them all, in general, as 401(k) plans. If you live in another country, please substitute your country's program in its place. Additionally, your country's specific plan may have differences to the American 401(k) plan, so this book may not accurately represent your situation. However, it will give you valuable information to use when you ask your advisors to determine the risks to which you are exposed. Educating yourself about these matters is a personal responsibility.

As you read this book you will also notice a fair amount of discussion about mutual funds. The reason for this is because the two go hand in glove. When you add money to your 401(k) account, those administering the plan most often invest that money in mutual funds. That's why it's so important for me to devote much of the book to explaining the weaknesses of the mutual fund system.

Armed with new knowledge and insights that you'll discover throughout this book, you will be better prepared to assess your own retirement situation and determine if your 401(k) investments are helping you achieve your retirement goals.

Be forewarned: This message is harsh and blunt. But it is vitally important.

I speak face to face with thousands of 401(k) participants each year as I travel and teach… so I know, first hand, the vast numbers of people who sense that something is wrong—terribly wrong—with the performance of their 401(k) accounts. They can't quite put their finger on it… but they can feel it. They *know*.

And for those of you who have been programmed to think that everything is okay with your 401(k)s… hold on tight. You are in for quite a ride… a no-holds-barred peek behind the curtain of what may well be the most outrageous act of robbery ever performed on the American public.

Chapter One

How Greed is Slowly Strangling our Future

If you currently have a 401(k) account—or some other type of contribution retirement plan found in almost every country—this may be the most important book you will ever read. There are hundreds of thousands of your dollars that hang in the balance. Your entire future, your goals, and everything you have been working for is at stake. There are no do-overs when it comes to your retirement. You only get one chance. This is something we must get right the first time around—because there is no second round.

You are about to discover one of the largest scams ever inflicted on the public. As you read this book, you will discover how these financial institutions, the institutions that we so easily trust with our money, have been robbing much of our retirement profits from the get-go.

And the worst part is: This robbery—all of it—is 100% legal. This means that these massive financial organizations have the blessings of governments to help themselves to our hard-earned money.

They lied to us about what we should realistically expect from these 401(k) plans. They lied to us about how much of our money they would keep as their payment for "managing" our accounts. They lied to us that we needed their expertise because it's too complicated for us to do on our own. And they continue lying to us by claiming it's our fault that our accounts aren't big enough to fund our retirement.

The 401(k) plan has only been around for one full generation of workers. But the results are already more dire than anyone ever imagined. And they'll continue to get worse over the next 10 to 20 years.

This is a story of the widespread havoc caused by the simple 401(k) system that everyone thought was their golden ticket to retirement. As you read about what is really happening to us, and what is being sold to us, you will probably feel a variety of emotions. Most of them are likely to be negative: anger, disillusionment, worry, and more. It's a natural reaction that happens when we discover we have been lied to so profoundly and that our trust has been betrayed.

When the ideas that would later give shape to the 401(k) plan were first presented to the American public, those ideas seduced us by painting a beautiful future where the money we invested would grow into a massive nest-egg. With financial freedom tucked away under the watchful eye of these trusted financial companies, we could turn our focus to working hard in the here-and-now. The future was taken care of by people smarter than we are and who cared about us. Eventually, we would count on our massive 401(k) savings to take care of us too.

But reality is proving to be entirely opposite than expected. That future we dreamed of is in serious jeopardy for most people. Millions and millions of people are now shell-shocked when they open their statements and see how their account has dwindled to just a fraction of what they were led to believe it should—and would—be as they approached retirement.

And the sad part is this: It's not their fault.

For most hard-working people, the near future only offers more of the same: more hard work. Out of necessity, they will continue working long into what they thought were their retirement years. Those dreams of traveling around the world are gone. So are the country club memberships. No leisurely days doing only what they want. No sleeping in. Instead, the alarm clock will continue to wake them up for another day of work… and another, and another.

Due to this massive nest-egg shortfall caused largely by misleading 401(k) promises, don't be surprised to see the target age for retirement continue to rise. For many people, retirement age will jump from 65 to 70, and then even 75. Could it go higher? Absolutely. And some people will never have the luxury of being able to retire.

This is especially true for those who currently consider themselves as being part of the middle class. In the past, working at a fast-food restaurant was the first job experience for many young people just starting out in the work force. Things are very different now, with some people forced to work in fast-food as the last stop on the employment train.

Even those who hope to remain on the edge of the upper class will find that to maintain their standard of living in retirement, there will need to be many more years of toil at the law office, making sales calls, or treating patients.

Most middle- and upper-class Americans don't expect the meager allotment they are scheduled to receive from Social Security to cover their living expenses. (I'll discuss this later in the book.) As these middle-class workers continue in the work force to maintain their standard of living, their expectations will also change. They will refocus their efforts on simply maintaining the necessities of life, while the dreams of living a comfortable retirement (with many of the luxuries they had anticipated) will, sadly, slip away.

How Did This Happen?

When you watch the news these days about this growing problem, you'll see something startling. The financial institutions are pushing the idea that the problem is our fault because we haven't saved enough money. Those words sound convincing when they come from the mouths of polished news anchors and respected financial commentators. But the truth is much different.

In fact, it all started as companies decided it was in their own financial best interests to shift away from offering the traditional defined pension retirement programs for their employees. Instead, they ventured onto a new path—with the government's blessing and the sponsorship of big financial institutions. That new path was to offer employees something new and totally untested: today's contribution retirement programs, most notably the 401(k) plan.

This massive change will go down in history as one of the most devious, immoral, and financially damaging campaigns ever waged against the middle-class worker.

In this book we will examine extensive evidence that our dire situation is the direct result of greedy institutions conspiring to take our hard-earned money without any care or concern about the consequences.

Please read this next sentence carefully. I do not believe that this coming disaster is something that *might* happen or that *could* happen—it is something that *will* happen. The 401(k) system is and will continue to be a failure if we expect it to provide the middle class with the retirement they deserve through their own hard work. It's that simple.

For those who understand the serious consequences of our society's aggressive shift to 401(k)-type plans, they can see it for the scam it really is. In spite of the fact it is entirely *legal*, this very real damage being inflicted upon people will probably be looked upon by future generations as one of the largest scams ever committed in this country.

There are very few voices trying to change this. And I'm one of them. I'm committed to doing everything I can not only to raise awareness of this legal robbery, but to give hope to those who have been victimized by the 401(k) system so there can still be a bright future ahead.

Money Machine Magic

In Las Vegas, there are thousands and thousands of slot machines. When you think about it, a slot machine is simply a machine that consistently transfers money from an individual to the casino. Based on math and statistics, the slot machine is programmed to win. Sure, you may 'win' a few dollars here or there. Some lucky soul may even hit the jackpot. But at the end of the day, the casino keeps a percentage of every dollar that is put into the machine. Everyone knows there is a lot more money going into the slot machines than coming out. It's that simple.

Gambler $$ ⟶ Casino $$$$$

Even though slot machines may be perfectly legal, that doesn't mean they are good, or positive, or uplifting, or fair, or moral. It's just a machine that has been given the official stamp of approval by the government.

Just like these slot machines, the 401(k) system is a very simple machine. It's a machine that consistently transfers money from your account to the financial institution that sponsors the plan in which you are enrolled. In an upcoming chapter we will reveal how the big institutions siphon off most of your earnings to keep for themselves. If you are like most people, you will be outraged by this discovery. Like the slot machine, your 401(k) plan is completely legal. Yet when you look at it closely, you'll see that it's a well-oiled money machine just like that slot machine. With slot machines, the casino is the winner and the gamblers are the losers. In the case of 401(k)s, the financial institutions are the winners and the investors are the losers.

Investor $$ ⟶ Institutions $$$$$

The amount of money that the financial industry skims from your account through their fees is staggering. In April of 2011, the Financial Times reported that the fund management industry is destroying $1.3 trillion of value every year. The article cited a survey conducted by the IBM Institute for Business Value that detailed staggering figures that demand our attention:

"The bulk of the value destruction, almost $1,100bn a year, equivalent to 1.9 per cent of global gross domestic product, is seen as impacting on clients. This includes $300bn in excess fees for actively managed long-only funds that fail to beat their benchmark (this figure is quoted as $834bn in the draft report but it is believed IBM has since revised it lower), $250bn spent in fees for wealth management and advisory services that fail to deliver promised above-benchmark returns, and $51bn in fees for hedge funds that also fail to deliver their targeted returns."

It's one thing to invest your money in something that is giving you value, but it's something entirely different to invest in something that actually hurts you financially. While we as investors focus on how our 401(k)s and similar accounts will help us retire with greater wealth, it's eye-opening to realize that the financial institutions are planning how they will grow their own wealth at the expense of our accounts.

In this book I will show you the very real and serious issues that a 401(k)- or RRSP-type plan presents. Along the way, I will invite you to ask yourself and your advisors some very direct questions. If you have the courage to seek the truth, I will give you the tools you need to question the chaos.

Since it's possible that you're unaware of the extent of this chaos, my goal is to help you understand what is really happening in the financial situations of people around the world. Then we will organize that chaos so you'll have a better idea of what you can do next. I hope this important information will balance the persuasive sales rhetoric about 401(k)s that seems to be everywhere.

I'm going to reveal for you some of the serious flaws of 401(k)-type plans without pulling any punches. I wrote this book to inspire you to become more determined to take the lead to build your own retirement, get educated, choose qualified advisors, and become financially independent.

Who Can Become Financially Independent?

You hear the phrase "financial independence" a lot, right? But what do we really mean when we say financial independence? Is it that point when someone has a high net worth or becomes a millionaire? In truth, net worth has nothing to do with financial independence. Think of it this way: If you had a source of income that provided you with more money that you needed to pay your bills and live your life, you would not need a job. With that in mind, perhaps it's more beneficial to set goals of building reliable streams of *passive* income, cash flow, from investments rather than trying to amass a large amount of money in an account like a 401(k). Only when our passive income exceeds our expenses can we claim the victory of financial freedom.

Because a 401(k) tries to build net worth rather than cash flow, retirees find themselves caught in a race against time. They must liquidate their 401(k) to cover living expenses that stubbornly rise year after year. They will have to reduce their standard of living again and again to stretch each dollar for fear of outliving their nest-egg. It's like watching two dwindling hour glasses: one filled with money and one filled with time. People will soon discover that their 401(k) turns out to be a small golden egg rather than a golden goose. When the egg is gone—it's back to work.

Two retirement strategies: the golden goose and the golden eggs

I like Dr. Stephen Covey's book *The 7 Habits of Highly Effective People*. In the context of building our retirement, let's review one of his habits and see how they apply to our retirement goals. Dr. Covey's Habit #2 is "Begin with the end in mind." This is sound advice for anyone's financial freedom project. Let me explain why: It's horrifying to think that we could work for ten, twenty, or even thirty years in a retirement program that is going to fail. So let's explore the 401(k) as a means of building retirement to see if it truly helps us achieve what we hope it can ultimately give us. That is what beginning with the end in mind really means.

Most people have heard of Aesop's fable of *The Goose That Laid the Golden Eggs.* In essence the fable tells a story of a goose that lays a golden egg each day. The owner of the goose becomes greedy and cuts open the goose to get to the eggs faster only to find that his greed has now killed the source of his magical income.

A golden goose is an asset that can produce a consistent cash flow we can rely on to help us cover all our living expenses in retirement. The story of the golden goose teaches us a very important lesson when it comes to preparing for retirement. That term is "passive income."

The Huge Difference Between Passive Income and Net Worth

It's unfortunate that so many people fail to begin with the end in mind when planning their retirement. The very fact that we often refer to our retirement account as a "nest-egg" illustrates that too many people are more concerned about their net worth than their passive income. Somehow that notion has dangerously embedded itself into our culture. And that misconception is ready to come back and bite us.

Each time the golden goose lays an egg it brings passive income to the household. One might look at passive income as the ability to generate "new money" without working each month, as opposed to relying on "old money" that had been generated years ago and placed in savings. The nice thing about having a golden goose is that as long as the goose is alive and healthy, there's potential for a lifetime of passive income that will never run out. Bills will be paid. Food will be provided. Clothing and shelter can be purchased. Healthcare will be paid for. But if the production of new money was to cease, then things change immediately. The moment the golden goose dies we start a race against time. Since there is no new money being generated, we are forced to draw on the old money that had been saved. At that point, confidence changes to hope. Now we are not certain of our future, so we cross our fingers and hope that we have enough golden eggs stored up to last our lifetime.

This simple fable is effective because it shows us the wisdom of finding and nurturing our very own golden goose. When we truly understand the fable, we clearly see that having the goose is more important than stockpiling golden eggs. You've seen those people who understand this principle, and you've seen the positive impact it has in their lives because they always seem to have more money than they need.

Defined Pension Plans vs. Contribution Plans

Chapter Four offers more detail about the shift many companies have made away from defined benefit pensions to contribution plans.

Remember, a defined benefit retirement strategy is like having a golden goose because the company you worked for sends you the money you need each month no matter how long you live. This is your golden goose.

In contrast, a contribution retirement strategy, such as a 401(k) plan, means you must save enough money to last throughout your retirement, however long that may be. It's a lot like saving golden eggs. If the eggs run out, then you are left with nothing to live on.

Let's look at them side-by-side to compare:

- A defined benefit of $6,000 per month provided by the former employer
- A contribution account that has a balance of $18,000

Defined Benefit Retirement

Month	Benefit	Expenses
January	$6k/Month Benefit	$6,000 required for monthly expenses
February	$6k/Month Benefit	$6,000 required for monthly expenses
March	$6k/Month Benefit	$6,000 required for monthly expenses
April	$6k/Month Benefit	$6,000 required for monthly expenses

Contribution Retirement

Month	Account	Expenses
January	$18,000 Account	$6,000 required for monthly expenses
February	$12,000 Account	$6,000 required for monthly expenses
March	$6,000 Account	$6,000 required for monthly expenses
April	$0 Account	$6,000 required for monthly expenses

What is most alarming to me is that I meet scores of good, hard-working people in their fifties or sixties that have *less* than $20,000 in their accounts.

How much new money can your 401(k) produce each month?

Now that you understand this golden goose principle, you might wonder how much money your 401(k) will be able to generate in new money when it's time for your old money to shoulder the burden of those stubborn monthly expenses throughout your retirement. Right now, much of your 401(k) money is invested in the bond market or the stock market via mutual funds. A long-term U.S. treasury bond offers a whopping rate of 2-3% as of this writing. Dividend yields from stocks in the S&P 500 index range from 6-8% on the high end to .1% on the low end, with an average of around 2%. If you have lost some of your confidence that you can count on stock market growth to provide consistent yearly capital gains to create income, you'll learn why you're not alone when you get to Chapter Three.

Financial independence defined

Financial independence occurs when you have a passive income that exceeds your expenses.

Financial Independence = (Passive Income > Expenses)

If your passive income is dependable and consistent, then you can live forever without working at a job. You can also endow your next generation with their very own golden goose.

The danger of living on a nest-egg is clear. Relying on net worth alone creates a race against time. Because without new money flowing in, the fortune is doomed to be spent down to zero.

A wise investor chooses to focus on creating a passive income generator, a golden goose, rather than on trying to pile up cash, golden eggs. Begin with that end in mind.

Financial independence as an attitude

Another way to think about financial independence is how much you depend on others for knowledge and decision making. In that sense, financial independence has less to do with someone's current financial situation and more to do with that person's *attitude* towards money. It's not about how much money you have in the bank. It's about how you view money, think about it, and ultimately understand how it works. If you currently rely on others for financial decisions, then you are "financially dependent"—even if you have all the money in the world. However, if you don't need the advice of others for your financial matters, then to a degree you are financially independent—even if you are starting today with very little in your pocket.

That's why financial independence starts with the right mindset, not the right amount of money. The first step to financial independence is a firm decision that you will live your life in such a way as not to be at the mercy of others. It's the pursuit of financial education and personal investing experience. It's a willingness to learn from the mistakes that will inevitably come along the way.

Taking responsibility for your own financial well-being is like learning to ride a bike. You may fall a time or two and get painful little scrapes, bumps, and bruises. Maybe even an occasional broken bone. But if you never learn to ride that bike, you're at the mercy of others as you sit on their handlebars totally exposed to the dangers of the road. When you allow yourself to be financially dependent on Wall Street's advice related to their 401(k) plans, the financial injuries you can receive at their hands can put you in the intensive care unit hanging on for your life.

With the right attitude toward financial independence, an average person with less than $1,000 can be financially independent. How? It's simple: If that person can invest their money—no matter how small—with confidence and direction… and without depending solely on a stock broker, banker, or financial advisor… then that person is financially independent.

The Danger of Being Financially Dependent

Now let's flip it around and look at the other side of the coin.

Financial dependence is born of ignorance. When you are financially dependent on others, you don't know what to do with your money. How many poor financial decisions are made in our society by people who simply don't know any better?

When you look closely at the situation, you'll suddenly realize that 401(k)s have created an entire generation of people who are investing without understanding. Even though we are a nation that is good at earning money, we have fostered an environment that stifles financial independence while growing the need for financial dependence. Look around your neighborhood. Chances are, most people depend upon a corporation or the government for their financial well-being. Sadly, however, the track record of these big institutions shows that they don't care much at all about our well-being. Instead, they are very much interested in growing, getting more power, and gaining more wealth—often at the expense of the individual who is reliant upon that organization.

It's good to have financial advisors and other trusted experts in your life. But when we hand over decision-making power we are handing over our financial independence. *We* need to be the ultimate decision-makers.

Again, financial independence is less about money and more about a person's attitude and education.

For Me, It All Started with the Dot-Com Bubble

We humans, by nature, are good at reacting to things that are happening to us now. Very few people have the time, energy, or vision to see how a new idea today can lead to problems down the road. For example, it would have taken a very sharp individual to foresee how the legislation that led to the emergence of 401(k)s—namely ERISA (Employee Retirement Income Security Act)—would become problematic 30-plus years later.

Most of us are just too busy with the everyday things in life. We don't have time to read the fine print of every new idea put forth by the United States legislature. For me, it took a very painful and personal event to alert me to what was happening all around us.

I first began to question 401(k)-type programs, and the mutual funds that make up the bulk of these investments, during the dot-com crash that began in March of 2000. In those days, I was just an average mutual fund investor like everybody else. And just like everybody else, my wife and I suffered some significant losses to our mutual fund investments in the dot-com crash.

What we began to realize was that the so-called diversification of mutual funds does not protect against a system-wide crash. For as long as we could remember, everyone had been preaching to us about mutual funds. We thought we were doing the right thing. But it took that crash to make us realize how vulnerable we really were.

I began to think about the whole situation in an entirely new way. And I asked new questions. If the mutual fund approach of the 401(k) system could leave me so vulnerable to a large crash, then why did the industry push mutual funds so hard? Why were they telling me that this approach would help me manage risk and diversify to prevent big losses when it was clear that the opposite was true?

The answer is simple. It's because 401(k)s and mutual funds create huge piles of money for these institutions. The 401(k) and mutual fund systems operate on greed. They do not operate on wisdom. They are finely-tuned, turbo-charged money machines.

The Devious Genius of Mutual Funds

As my wife and I began to look closely at the many mutual funds that made up our retirement accounts, one thing became very clear to us. We realized that the stocks held in most of these mutual funds were very basic "no-brainers" you could read about in financial newspapers and magazines. We were not convinced there was very much research or expertise involved at all. I still remember feeling that I could have picked those same stocks myself, even though I knew almost nothing about stocks in those days.

In looking at the specific stocks those mutual funds were buying, I saw companies such as Nokia, AT&T, Enron, and other big names. During those years, these were high-flying stocks everyone knew about. They were the stocks everyone wanted to buy. Where was the genius in that on the part of the mutual fund companies? Suddenly I realized there was no measurable value in the analysis influencing their stock picks. Instead, the genius of mutual fund companies was focused on something entirely different: How to take money from my account with as little work as possible.

That experience was the painful kick in the pants I needed to improve my own financial education. It was also the beginning of my research into the 401(k) industry and the mutual fund system as a whole. The more I discovered about how these companies operate, the more disgusted I became. As I uncovered statistics and reports, and applied a bit of common sense, the picture became very clear to me. It seems the mutual fund industry is more about making money for the large institutions than it is about making money for the investors—people like you and me. But that's only half of it. The laws put into place by our legislators to make 401(k)s possible also acted like fertilizer for this industry and it's grown like crazy. It didn't take long for me to understand why that fertilizer smelled like it came from a bull.

Selling mutual funds became extremely lucrative for these institutions and the industry absolutely caught fire. Unlike hedge funds, mutual funds could aggressively advertise for new investors. As they flexed their marketing muscles, the money came rolling in. And it still rolls in today. As I've stated in the beginning of this chapter, companies that promote their mutual funds and 401(k) programs have a powerful money machine. When the money flows in so fast, the perspective of the funds can easily become skewed and distorted. The focus can shift from serving the fund's investors—you and me—to serving themselves—the managers and institutions.

Part of the marketing message put out by these huge financial institutions is that they have the experience and expertise to help grow your money. But the more I study the industry and how these companies operate, the more I am convinced that mutual funds and 401(k)s were created chiefly to make these institutions rich.

How Big Is Big?

To measure how much wealth a country is producing, economists add up the value of all the goods and services created in that country during a given time period. It's called Gross Domestic Product (GDP). In a 2010 study, the Securities Industry and Financial Markets Association reported: "The wealth generated by the financial services industry contributed nearly 6 percent, or more than $828 billion, to 2009 US GDP." With that kind of money at stake it's no wonder these institutions are competing aggressively for their share.

How long will it take before the world realizes that these retirement plans were not created to solve their retirement problems? When will it become clear that these are the inventions of people who saw an opportunity to make a lot of money by creating wide-mouth funnels that would continuously pour money into their own bank accounts at the expense of honest, hard-working people?

John Bogle is a legend in the mutual fund industry and is the founder of Vanguard, one of the largest mutual fund companies in existence. In 2006, Bogle wrote a scathing letter to the SEC (Securities and Exchange Commission), the government body that oversees the investing arena in the United States, regarding the shift from wisdom to greed that has occurred in the mutual fund industry. He called for improved regulation to help prevent the abuse of investors by fund managers. Among his many chastisements was this statement that gives a clear and appropriate summary of the situation:

> *"I have many concerns about the prevailing levels of conduct and values in today's mutual fund industry. But my over-riding concern is that funds are operated largely in the interests of their management companies, rather than in the interests of their shareholders."*

Why is my money being invested with companies that create a system that ignores my goals?

Wall Street greed is nothing new, of course. It really shouldn't be surprising to learn these things because the public is already suspicious of Wall Street. Based on past actions, it's reasonable to be suspicious of their motives. From Eliot Spitzer's attack on mutual fund scandals to more recent headlines exposing guys like Bernie Madoff, it's definitely not unusual to find greed as the main goal for these people. What is so shocking is the amount of lies and deceit being fed to us.

You Are Sitting on a One-Legged Stool

When the 401(k) plan was first introduced, it was never intended to shoulder the entire burden of your retirement. In fact, back in the late 1970s people often talked about the "three-legged stool of retirement." These three legs were: (1) the employer's pension plan; (2) Social Security benefits; and (3) personal contributions.

We will explore this topic in depth later in this book, but I think it deserves a brief mention here. In a nutshell, this three-legged stool is getting very shaky. Thousands of companies have eliminated their pension plans. Social Security is on very thin ice, and most people who are due to retire in the next 10 to 30 years don't expect to receive what they were promised from this forced savings program.

Now it looks like the third leg of that stool, the personal contributions to the 401(k) plan, is being forced to take on all of the responsibility for your retirement. The problem is that even in the best of economic conditions your 401(k) plan simply cannot grow enough to give you the amount of money you deserve when you retire.

And the problems don't stop there, because we are NOT in an ideal economic situation. We have been hit head-on by two strong market crashes in recent years. The economy is stagnant. Market growth is relatively flat as it continues to try and dig itself out from those two crashes. On top of that, the debt level forced upon us by the federal government has put all of us at the cusp of yet another bursting bubble that will push the markets even lower for a longer period of time.

If it's not clear to you how this will seriously damage your retirement outlook, consider this:

- Your 401(k) account will only increase in value if the market goes up. If you're like most people, your account is still recovering from the market crash in 2008. As the dollar continues to get weaker because of our massive government debt, the market will eventually crash again. Your 401(k) account needs plenty of time and big market gains to do its part in helping to fund your retirement. However, time is running out as the overall economy continues to be shackled by debt problems that will not go away anytime soon. And it's not clear when the market can break free of these bigger economic issues to give your account the big gains it is craving.

- Another side-effect of the dollar becoming weaker—which it will—is that inflation will rise. Why is that a big deal? Because when it's time for retirement, you'll need to determine if your 401(k) account will be big enough to cover the steep price increases that inflation will bring. For example, will you be able to afford $10 per gallon to fill up your gas tank? Will you be able to enjoy a healthy salad at $5 for a head of lettuce and $2 for a tomato?

When you look at the inherent problems with 401(k)s, and then put that problem into the context of the bigger problems facing our economy, it's easy to get overwhelmed. It's chaos within chaos. It's like trying to board up your house with a broken hammer to protect it from the coming hurricane, only to find out you don't have nearly enough nails and plywood, and the hardware store is long sold out. You know you need to do something, but it seems you are all out of options.

These coming storms have a profound impact on economies at the national level. But with their 401(k)s and mutual funds exposed to so much more risk and downside potential, I'm frightened to think of the effect they will have on hard-working individuals and their families.

The effect that 401(k)-type plans will have on the middle class will grow to become one of the next major financial tragedies we will face. It's looking at us square in the eye today. Even though contribution retirement plans are legal and growing, they will fall apart in the same way that many illegal scams do. Unfortunately, it's the little guy who will suffer the greatest injuries.

The 401(k) system will eventually cause massive problems for the stock market and for the average retirement plan participant. But there can be light up ahead for people who make wise decisions.

We will see that this storm doesn't have to be a frightening surprise when it really hits hard. That's why we will look seriously at why you and

I now need a more comprehensive financial education to survive and even thrive when the rain and winds come at us full force.

The Real Problem Is Ignorance

The SEC does its best to regulate the industry and protect investors. They conduct investigations as they work hard to look out for the little guy. They prosecute those who are shady business people. However, there is one thing I have learned through my research and as I've pursued my own financial education: *It's impossible to truly protect the ignorant.* Congress can pass laws all day long, but those laws will not make people smarter. It's up to us individually to improve our own financial intelligence. Greedy folks will find ways both within the law, and outside of it, to pick our pockets. The only person who can protect your money from these sharks is YOU. Laws and regulations are no substitute for experience and education.

One goal of this book is to help you learn to ask the hard questions of your advisors. I also want to help you analyze your own situation to determine if you are invested properly to achieve your personal goals and objectives. Armed with this knowledge, you and your advisor can work together more effectively as a team to truly improve your investing approach.

What's More Important: Investment or Investor?

If you listen, you'll hear a lot of people ask what type of investments they should have:

> *"Where should I put my money?"*
>
> *"Are stocks safe?"*
>
> *"What about options?"*
>
> *"Or should I dollar cost average with mutual funds?"*

At this point I think you understand that these questions are way ahead of themselves. If all these people are concerned with is where to put their money, they are destined to be financially dependent on others.

The correct question, of course, starts at the beginning: *"What type of investor do I want to be?"* That's the first question that a person should ask when they want to become financially independent.

But what happens when we talk about investments? Whether it's on financial TV news or talking with a friend, the focus is typically on how "aggressive" or "conservative" a particular investment appears to be. All the while, the conversation totally ignores the financial education level of the investor.

How important is education if your goal is to minimize risk and maximize safety?

Consider this statement: "We should all drive cars or ride bicycles because traveling in airplanes is too risky."

I frequently ride on airplanes as I travel around the world teaching people how to become smarter investors. I also have a family that I love very much. That's why I respect the education that the pilots go through to earn their wings. I respect the experience they have flying that airplane in all sorts of weather conditions. The last thing I would ever do is jump on a plane with a pilot who has never flown. The difference is the education they have gained. I always want to be on the side of education, because it's my best chance of staying safe and prospering.

As I mentioned before, the 401(k) has been presented as a plan that will help you get what you want, a big bank account when you retire, with zero work on your part. In other words, the 401(k) is a way for the financially uneducated to buy investments without becoming educated investors. I have learned through hard experience that there is no such thing as a shortcut to being a good investor. I'm still learning more each day. When you give your money to someone else to invest for you, you are not an investor; you are a spectator. When you buy a courtside seat to an NBA basketball game, you are not part of the team; you are a spectator. When you go to a concert, you are not the guitar player; you are a spectator.

As you continue reading the eye-opening revelations in this book and become more educated on the issues facing 401(k)s, RRSPs, and mutual funds, you will probably find yourself wondering what you should do in the light of this new information. When you reach that point, remember to ask yourself the right question: "What kind of investor do I want to become?"

At this point it's not about *where* you should invest your money. It's about giving yourself the right financial education. It's about gaining the knowledge and skills you can use time after time to help you truly become financially independent. Becoming financially educated is a process and does not happen with one book or one conversation with your advisor. It takes time, effort, and experience. But it will come. And that commitment to financial education can pay you rewards that are greater than virtually any other type of education.

Armed with an honest, hard-earned financial education, you are less likely to become a victim of what I call "The Ignorance Myth."

Chapter Two

The Ignorance Myth

One of the worst side effects of the 401(k) system (and similar programs around the world such as Canada's RRSPs) is that they have convinced us that it's okay to be financially dumb. Millions of people have heard that seductive song and now believe they can become rich in their financial ignorance. But it's a complete and total myth that is costing those people untold billions of dollars.

Look at it this way: When putting money into a 401(k), people give up a significant amount of control to the mutual fund managers they have never even met. They don't know anything about them. Yet, as we have shown, those faceless managers are responsible for your level of comfort during retirement. When you think about it like that it doesn't make very much sense, does it?

The whole scenario is like believing that you can become an accomplished musician by having someone else go to piano lessons for you and do hours of practice—while you watch TV. It cannot be done. You can't have someone else exercise for you and expect to become fit.

But the facts are clear. There are millions of people who are investing in their 401(k)s but know nothing about how these investment plans work, where the money goes, what kind of crazy fees they pay, the tax consequences, the risks they face, or even how much money they will need for retirement. They simply have the money automatically withdrawn from their paychecks because they are told by the financial institutions and their employers that it's the smart thing to do.

Take a moment to think about it. How smart is it to enter into an investment without knowing anything about it?

Would you feel comfortable buying an apartment building if you knew nothing about real estate?

Would you risk a million dollars buying a franchise if you knew nothing about business?

Of course not.

Yet somehow we have been brainwashed into accepting an equally ludicrous scenario with our retirement investments. We are betting our entire future on these unknown advisors who will guide us through Wall Street. Yet we have virtually no education on stocks and mutual funds.

Awareness Is Not Proficiency

A common trap that many people fall into is that through their own arrogance they confuse gaining an initial awareness of basic investing strategies with being a proficient investor. Confusing awareness with proficiency is extremely dangerous!

For example, I may know what a mutual fund is. I may understand how the money is pooled by thousands of investors and managed by a team of so-called experts who send out statements every month. But does this basic understanding mean I'm actually good at investing in mutual funds? No, it does not. I know what a scalpel is, too. But it's safe to say that with my current lack of knowledge regarding surgery, I'm not ready to cut someone open.

The introduction of the 401(k) brought with it an era of oversimplified investing. We seem to think that with an automatic payroll deposit into our 401(k) account our hands are clean of the dirty work of investing. But here's the problem: When we deal with our investments only at arm's length, we fail to give the market the respect it demands.

Have you ever heard the market described with words such as:

- Ruthless
- Unforgiving
- Unpredictable
- Corrupt
- Speculative

The truth is, all of these words are accurate when used to describe the market. As we become aware of what the market really is, we can prepare our minds to learn how to deal with it. We don't have to be intimidated by these market characteristics. We just need to understand how to control them to our advantage.

Now take a moment and use your common sense to think about this question. Is it a sound idea to place virtually all of your retirement money into a program you know very little about?

The Education Continuum™

Over the years I've helped thousands of people successfully navigate their path of financial education. Though everyone is unique, the journey is very similar for virtually everyone as they progress through specific milestones on their way to investing proficiency. To help student investors understand and chart their progression, I have developed what I call The Education Continuum™

Too often we mistakenly equate "ignorance" with "lack of intelligence." In truth many 401(k) participants are highly intelligent and hold advanced academic degrees. In this case "ignorance" simply means the person has not focused his or her genius to the area of knowledge in question. Investing in a state of ignorance intuitively feels like a disaster is waiting to happen. Sadly, most 401(k) investors are at that level.

Look at The Education Continuum™ and try to honestly assess where you are in regard to your understanding of investing:

Awareness might be described as knowing what you don't know. In that situation, at least the person knows what to study and better understands the right questions to ask.

Competency might be compared to an airline pilot who can pass a written test of flight regulations and procedures, but has not yet logged any time in the air. As collegiate basketball players, my teammates and I could easily diagram every detail of the offense and readily answer any question posed regarding the play book. But the actual execution of the game-plan in a hostile environment, under pressure, is a very different story.

I believe that consistent, passive income is achieved with investor proficiency.

Many people have lifestyle goals. They might set a goal to get a certain sized house or drive a specific model of automobile. Some investors have money goals, be it a passive income goal or even a net worth goal. But how many investors have education goals? Life style comes from money, but money comes from financial education. Consider this truth: We are likely to achieve our lifestyle and money goals if we first set and achieve our investor education goals.

Don't Just Have Investments – Be an Investor

One of the most common mistakes new investors make is that they focus on what they want to own rather than what they want to become. A person with no knowledge or understanding can own investments. But proficiency suggests that someone has the ability to take the right steps to achieve specific, desirable results.

As you concentrate on growing your knowledge of investing through education, you will enjoy becoming more *aware* of the investing techniques people use in the stock market to achieve monthly cash flow and retire early. In time, you will not only realize that it can be done, but that you can become *competent* in how to invest intelligently for your own success.

The ultimate goal is *proficiency*—the ability to take the right steps that lead to the desired results. Those who are proficient have become investors, while those who fall short of proficiency merely have investments and must depend on others.

Lack of Knowledge Forces You to Depend on Someone Else

Imagine you are placed in the middle of the woods with another person you have never met before. You are told that it takes one day on foot to get back home. You are given a map, a compass, and just enough food and water for one day. Your companion has the same. The map shows where you are, and where your home is. But you have never used a compass before and you're not sure how it works. The other person claims to know how to use the compass and offers to guide you to your house.

When we can't do something for ourselves, we are forced to rely on others. And when we rely on others, we are also surrendering control to them. Do they really know how to use a compass and read maps? Do we trust them to lead us safely out of the woods? Are they most interested in helping us, or themselves?

Because of a lack of education, many people have become totally dependent on outside advisors, such as their 401(k) companies, to take care of their money. They depend on these unknown advisors to make their dreams come true.

Perhaps we are so trusting of these faceless financial advisors because of an illusion that has been created. There is a perception that they possess almost magical predictive powers far beyond our own abilities, even to the point of, supposedly, seeing the future. Even more, we are made to feel that these special powers are beyond the reach of ordinary mortals like you and me. It has come to the point where our culture just assumes we can't learn these skills for ourselves, that we can't do the "magic" that they do. So we quietly kneel before the 401(k) companies and lay our futures on their altars, completely at their mercy.

What Skills Do You Really Need?

When I talk about the topic of our growing reliance on others, some people naturally respond by saying, "How can I possibly learn to manage my own money? There aren't enough hours in the day!"

This is a very important question, so let's look at it more closely. Our lives are filled with tasks that need to be done. A typical day is filled with a series of tasks. Most of these tasks require very little skill while some require more skill. Over the years, we come across a few situations that require skills of a very specialized nature.

Let's create two categories for these skills we need during our lives:

1. Life Skills
2. Skills for Hire

As we live our lives every day, we are mentally assigning the skills needed to the tasks we face on our path. For example, one task is that we need to go from home to work and then back home again over the course of a day. How do we travel those distances? One option is to hire someone who has the skill to drive us everywhere. Another option is to acquire this life skill for ourselves and remain in control of our personal travel. We could hire someone to tie our shoes for us, or call it a life skill that we learn… a skill that gives us the power to do this on our own.

Obviously, there are some skills which are very difficult and time-intensive to acquire. In some of these cases, the smart thing to do is hire someone who has dedicated their life to becoming an expert at that one specialized skill.

It begins to make sense when we can separate these tasks and skills into the two categories we discussed above:

Life Skills	Skills For Hire
Read and write	Edit my books
Brush my teeth	Perform my root canal
Clean my house	Build my house
Drive my car	Fly me to Hawaii
Raise my children	Deliver children (birth)

Can you see the difference? Learning good life skills will help us navigate through everyday life with a minimum of fuss. We barely think about these life skills because they are second nature to us. But when a big issue arises—especially a life or death situation—which requires a heightened level of skill, that's the time to hire others to do the job properly.

When it comes to investing, many 401(k) investors have decided to put investing into the "Skills for Hire" category rather than the "Life Skills" category. This is what the world famous investor Warren Buffett has called "the ultimate irony."

The Ultimate Irony

The 401(k) culture promotes the idea that only the "experts" on Wall Street have the skills to invest safely and profitably. Quoted in an article in *CFA Magazine,* Warren Buffett disagrees:

> *"The ultimate irony of the investment business is that there is no question that an obstetrician can deliver babies better than the husband or wife. If you take dentists as a whole they will pull teeth or fill teeth better than if the patient does it themselves. But in the investment world someone who believes in American business and is consistent will get results that exceed professionals as a group.*
>
> *"It's the only industry I can think of where the professional's efforts subtract value from what the layman can do himself."*

Examining it more closely, the 401(k) culture robs us of the experience, satisfaction, and financial rewards of becoming serious investors. If we don't care about our money and don't care about increasing wealth for the future, then it's fine to hand it off to someone else.

Having money is sort of like having children. My children are mine, and I'm responsible for them. If I pass off the entire responsibility of raising my children to others, I rob myself of finding out just what kind of father I might have become. Will my children be taught what is important to me? Will they have the values and morals I want to pass on to them? I have no idea, because at that point I have given up control of their upbringing.

Obviously, there's nothing wrong with services such as day care to help out. We all need some help along the way. Ultimately, though, I'm the dad. Moreover, even the best day care folks do not have the same feelings for my kids that I do. The same is true with your money. No one cares about your money like you do. (Except maybe the tax man.)

When we have money in our hands, it is our responsibility to spend it wisely and invest it without ignorance. Just as with raising our kids, it can be valuable to have an advisor help us along the way. Even with the help of an advisor, we are each ultimately responsible for what happens to our own money.

Remember: No one else will care for our money like we will. But 401(k)s and mutual funds encourage a very hands-off approach. They are mostly out of sight and out of mind. Sometimes our only reminder they exist at all is the quarterly statement we get in the mail. Even then, we rarely use that information to take any kind of action. The statement may deliver good news or horrible news, but in either case most folks don't do anything to change their strategy.

Because of how we have been trained on what to think and how to act, our long-term investing plan typically looks like this:

Work and buy mutual funds…
Work and buy mutual funds…
Work and buy mutual funds…

This is a fantastic strategy—if you are selling mutual funds.

This robotic and mindless blind faith in the long-term performance of the stock market is spun and twisted with phrases such as "being patient" … "being consistent" … "not panicking" … and "staying the course." These words sound good and feel good when we hear them. But this sense of safety is based on false premises and false promises.

If you were standing inside of a burning building with fiery beams and rubble falling all around you, would you be willing to remain patient, be consistent, avoid panicking, and stay the course while waiting for something to magically transport you to the safety and fresh air that is available outside? Of course not! When you see danger, you do everything you can to stay alive. You run away from the danger as fast as possible. Waiting around and hoping the fire will extinguish itself isn't smart or prudent, it's just foolish. It's like sitting in the dining room of the Titanic playing cards and as the water rises, saying, "Gee, I hope this situation improves in a little while."

Make Investing a Life Skill

We can be more than simply a worker bee in life. We have amazing brains that can learn new things and acquire new skills. We can be men and women of many talents. We have the capacity to learn things that can be valuable to us. We can develop hidden talents when we decide it's important to us.

Take the example of a young man I know who has become quite an accomplished pianist. From age 8 to 18, he spent 30 minutes each day learning to play the piano. When you add it up, that's almost 2,000 hours spent on that piano bench. He also took lessons once a week that cost about $20. That's nearly $10,000 invested in just his musical education. He wasn't born with that skill, but with a committed investment of time and money it became a reality. Today he can make beautiful music that blesses his life and those around him.

We can do the same thing as investors. If generating money through investments is important to us, we can acquire new skills that will bless our lives with freedom, time, and great satisfaction.

Just as people take lessons to play a musical instrument... learn to prepare a gourmet dish... or take a motorcycle safety course... you are allowed to invest a little time in learning new things after the formal 'education' of high school and college.

However, people are less likely to search for solutions if they do not know there is a problem. That is exactly why this book is so important. Just as I'm dedicated to helping millions of 401(k) victims better understand the problems that loom ahead, I have an even greater passion for teaching thousands and thousands of people the basics of the stock market, risk management, and cash flow. These are concepts and skills that can transform your life.

Ponder these words from Emerson:

> "*That which we persist in doing becomes easier for us to do; not that the nature of the thing itself is changed, but that our power to do it is increased.*"
> *– Ralph Waldo Emerson*

Again, the culture of the 401(k) system has trained us to think we can't become good investors on our own. If this continues, the system will continue to breed less intelligent and less successful investors. We run the risk of becoming voluntary slaves to a financial system that takes our money and leaves us with a bit left over. In other words, we are heading down a path that is the opposite of Emerson's statement:

> *That which we resist in doing becomes harder for us to do; not that the nature of the thing itself is changed, but that our power to do it is decreased.*

Vital Lessons on Ignorance from the 2008 Subprime Crash

I remember the first time I was introduced to some new kinds of mortgages that began popping up several years ago. These zero-down mortgages came on the scene and provided a way for people who had no savings for a down payment to move into their dream home. Additionally, stated-income and no-doc loans allowed borrowers to sign on the dotted line for huge amounts of debt with no significant proof they could make the payments over the long term. The nail in the coffin on these mortgages was found in these three letters: ARM.

Adjustable Rate Mortgages (ARMs) baited these eager buyers with a low, teaser rate on the mortgage for a few years. Then disaster struck. After the initial low interest period, the higher interest rate kicked in and pushed the monthly payments beyond the ability of most families to meet the unexpected hike and obligation. Many of these people were already living paycheck to paycheck. This huge increase in payments was more than they could bear. Interest-only and option-adjustable mortgages gave subprime borrowers the privilege of home ownership before it was earned or deserved. The lenders were greedy to get the loan business, and buyers were greedy to get the house they had never been able to afford before.

At the time, I remember thinking that these were very foolish mortgages and I watched some of my friends hastily hop on the house-flipping bandwagon. I saw others buy lavish homes that were stretching their incomes. For many of these people, it didn't take long before the "For Sale" signs went up and they were forced to lick their financial wounds. The mortgage system teased them in and then set them up for failure.

In a fair world, these people would be left on their own to deal with the consequences of their decisions. But in our interconnected financial world, it doesn't work that way. Instead, here's what happened: The collective mass of all the subprime mortgages added up to a weighty problem that would crush the entire financial system and bring dozens of banks to their knees. The government then used *our* money to bail out the banks that were responsible for initiating these bad loans in the first place. In short, the problem grew from the poor decision of individuals into what is called a full-blown "systemic problem."

How a Lot of Little Problems Will Add up to a Really Big One

The resulting subprime meltdown was a result of the chronic greed of the big financial institutions compounded by the ignorance of the individuals who were sold unrealistic mortgages that they did not understand and could not afford. The greedy prey on the uneducated, the same way a lion singles out the young and the weak. These people would show up at the title company and sign a huge stack of documents that were camouflaged in legalese and confusing financial jargon. They did not have a clue about what was going on. Furthermore, they didn't have an advisor on their side who could realistically explain what they were getting themselves into.

It is a shame that we are not given a true financial education in high school. As a result, most of us are left to make important investment decisions throughout our lives without knowing the possible consequences of those decisions.

With the subprime meltdown, the hungry institutional lions preyed on uneducated borrowers. With 401(k)s, these institutions are turning their hungry fangs to the uneducated investors around the world.

When I teach investors around the United States, I'm shocked that less than 20% of the people I speak with understand the mandatory distribution of their 401(k) that begins at age 70½. Even fewer can articulate the difference between the defined benefit plan and a contribution retirement plan we discussed briefly in the last chapter. I see a lot of similarities between the people who did not understand their subprime mortgage and these folks that don't understand their 401(k)s. It is tempting to lazily ignore the lessons of the subprime mess and once again say that these people will have to sleep in the bed they have made. And it's tempting to say that survival is for the fittest. However, this is another situation that will affect all of us. Just as in the subprime mortgage mess, the ignorance of many single investors will create a tsunami of consequences that will rock the whole system, and one that could be far more severe next time around.

Here is a huge lesson: Just as the subprime loans created a false supply and demand bubble in the real estate market, the same is happening now in the stock market. People are not necessarily buying stocks because the companies are solid investments. They are buying stocks because they are on a schedule to do so. The money flows into their 401(k) plan, and the management company is going to buy mutual funds with that money, which then triggers the mutual fund company to buy more stocks with the new money. And in the not-too-distant future, they will begin selling for the same reason. When you factor in the nature of liquidity in the stock market, we have a massive time bomb that is ticking and ready to explode. We will learn more about this time bomb in a later chapter, a chapter named after Robert Kiyosaki's eye-opening book, *Rich Dad's Prophecy*.

Some Financial Advisors Want You to Stay in the Dark

The ignorance myth also helps some so-called experts thrive. As long as people are handing over control of their financial future to others, then advisors such as financial planners and stock brokers will have a lot of job security.

Please don't misunderstand me. There are good advisors out there who are willing to work with hands-on investors. It just takes a special breed of advisor because it requires a lot more work for them to give you the help you deserve.

For financial advisors, though, it's much easier, and often professionally safer, to advise clients to conform to their own pet strategies than to create a strategy that fits a client's goals. Taken to the extreme with a 401(k) plan, there is no individual strategizing at all. Within your plan, it's typical that your only options are to choose from among boilerplate plans One, Two, Three, or Four. That kind of push-button investing doesn't make you smarter. Even worse, it doesn't require any expertise from your 401(k) company.

As long as people remain in the dark about how to take care of their own money, they will probably never demand anything more than what they are getting right now. We have become trained to accept whatever these companies give us. The longer they can keep us uneducated, the more money they will make. It's the perfect business model if you're in the 401(k) or mutual fund business. In the coming chapters, I will show you that, in most cases, it takes almost zero expertise to manage these funds, since they are typically tied to the overall stock market—or a specific portion of it. This means they are betting your future on the luck of the market with virtually no additional management to protect your investment.

Our Worst Enemy Isn't Ignorance – It's Apathy

Worse, perhaps, than not understanding how 401(k)-type programs work is when someone doesn't care about what's really happening to their account. Isn't it a lot easier to go to pick up the mail, pull out another quarterly statement, shake your head again at the poor results, and do nothing about it... than to contemplate the alternative?

Because, on the other hand, asking tough questions about those poor results and seeking for new answers can be a little more difficult and time consuming.

Apathy is easy, but can cost you a bundle in the long run. Is it because we're lazy? Or maybe we think that somehow a hero on a white horse will ride in at the last minute and add several zeros to the numbers on that quarterly statement? In this story, there is no savior but you. No one but you has the reasons and motivation to change the way the story ends.

If we can somehow get past the apathy that is holding us back to proactively take care of our own money, there are a few different paths we can take.

- We can try to change the system, or
- We can change ourselves

To me, it's obvious that the best path to take is to change ourselves. Why? Because no matter how much we dislike the current retirement investing system, it's unlikely we can make serious changes to the system in our lifetimes. These massive institutions have almost limitless resources to keep the government from changing the rules.

The way to win is to learn to play the game a better way. Better not to worry about trying to change the game—just learn to play it well.

A tremendous eye-opening experience is when we realize that there are things we can control and others we cannot. This realization is helpful for those working to break an addiction. I admire how people in those situations turn to the lesson of the serenity prayer:

> *God grant me the serenity*
> *to accept the things I cannot change;*
> *courage to change the things I can;*
> *and wisdom to know the difference.*
> *– Reinhold Niebuhr*

Yes, it's easy to get on the blame-the-government bandwagon. It's easy to hang out with your friends and curse Wall Street. Ultimately, though, blaming and complaining will not improve your situation. You may have a valid point and your complaints may be justified. But complaining will not help you fix your own retirement problem, and it does not solve the Ignorance Myth.

As I've explained earlier in this book, defeating the Ignorance Myth will not come through legislation or whistle blowing. Instead, victory comes person by person. It is an individual battle. And we have to choose for ourselves whether or not we are willing to enter that battle and win.

Ignorance Puts You at Serious Risk

The last thought I want to leave with you in this chapter is straightforward: What you don't know CAN hurt you—and probably *will* hurt you at some point.

This is especially true of investments. The people with the most knowledge attract the most money. The people with little knowledge will lose the most money.

Placing our money in investments we know little about, such as 401(k)s and mutual funds, means that we are giving up control. And giving up control puts us at risk. In the next chapter, I will show you one of the main reasons why I believe 401(k)-type programs put us under more risk than the average person ever imagined.

Chapter Three

Swimming in a Sea of Risk

We just revealed the lie we've been told, that it's possible to become wealthy through ignorant investing. This lie is the basis of the entire 401(k) and mutual fund system.

Now let's reveal another common lie that is just as dangerous to our financial future. This big lie is that we're told the investments which make up our 401(k)s and mutual funds are "conservative" and "less risky." I have even heard people talk about their mutual funds as being "safe" investments.

If we are serious about growing our investments and at the same time protecting our accounts from losses, then it's time to open our eyes. We're about to see that there is nothing safe about these hands-off investments.

There Is No Such Thing as a Risk-Free Investment

If you have ever made any kind of investment, you probably put your signature on a document that confirms you understand that investing carries various inherent risks that could result in the loss of some or all of the money invested. As I talk to people all over the world, I don't think most investors are taking this as seriously as they should.

It seems that most people are only slightly aware of the risks that exist when they sign those disclaimer documents. I don't believe the average investor understands how significant those potential risks may be. Moreover, they don't appear to understand the very real chance that their investment can lose much of its value. That's what is happening all over the country right now. The worst-case scenario is playing out in the lives of millions of people. The hidden risks—the downsides they never took the time to learn about—are happening to their investments in real life. They are losing huge amounts of money and time at the worst possible point in their lives. And they didn't even know it was *possible* for the risk to hit them like this.

Diversification Gives You More Ways to Lose

When you listen to the "experts" who promote 401(k)s and mutual funds, they are singing a pretty lullaby about safety with a song they call diversification. They must be good singers, because this song about diversification has been at the top of the charts for a long time. It's been popular for so long that nearly everyone knows the words: "Diversification equals safety." There's just one problem: It's totally wrong.

Look at it closely and you'll see that even when you enter these "safe" investments they sing about, you still must sign the same disclaimer with the same fine print—which means you are indicating you understand that you can lose some or all of your money with their investment plans.

Consider the concerned person who goes in every year to get his flu shot. Because he wants to stay healthy, he may ask to receive multiple flu shots just to make sure he doesn't get sick. With several flu shots in his arm, he has a false sense of security about his health. Why? Because he has only solved one possible illness he may contract. By focusing all his attention on the flu, he has totally ignored the risks of other diseases such as smallpox, polio, typhoid, and countless others that may be out there. Is he truly at risk of getting some of these other diseases? He doesn't know until he realistically looks at his own situation and then makes an informed decision.

It's the same for an investor. Diversification is a tool that really only addresses one kind of risk, called "non-systemic risk." The problem is, diversification can be a sitting duck for other kinds of risk that can be devastating to your accounts.

Non-Systemic Risk

Non-systemic risk is something that can happen to only one company at a time—not the whole stock market system. As a result, only that one company's stock price is affected by that event. For example:

- A CEO gets indicted for fraud.
- An auto manufacturer must recall thousands of automobiles because of a defect.
- An oil company causes an environmental hazard in the Gulf of Mexico.
- A pharmaceutical company fails to gain FDA approval for a new drug.
- A technology company fails to meet their earnings estimate.

These sorts of things happen from time to time. But they rarely have a negative impact on the overall stock market. Instead, the impact is felt on that individual company's stock price. It might go down, and then it may go up again.

In the spring of 2010, British Petroleum (BP) shares were flying high around $60 per share. Little did we know that BP would soon stand for "Broken Pipe" due to one of their oil rigs springing a leak and spewing huge amounts of oil into the Gulf of Mexico. By the end of June, the share price was cut in half.

If you had invested all of your money on that one stock, you would have lost half of your investment.

These types of risks are often impossible to foresee. That's when the typical financial advisor will say, "You shouldn't have all your eggs in one basket. You need to diversify!"

The idea behind diversification is simple: If we spread our investment money around with a lot of different companies, hopefully the profits we earn from the good companies will be larger than the losses from the few bad companies in our basket. This idea of spreading our money around multiple companies is called diversification, and its main attraction is to address non-systemic risk.

But what happens when there is a problem with the overall market? What happens when the market drops by half over the course of a year? In most cases when you are invested in mutual funds and 401(k) plans that follow the overall market, you are in big trouble. Because all of your diversified stocks will go down with the market. Some might go down a little, others might go down a lot. In the end, your diversification plan left you with a massive weak spot called "systemic risk."

Systemic Risk

Simply put, systemic risk is what happens when an event rocks the entire system.

Diversification does not protect investors against systemic risk. In fact, it's easy to argue that diversification exposes you to more systemic risk. It was a systemic problem that caused investors to lose 40-50% of their retirement money parked in their 401(k) in the subprime crash of 2008.

The subprime crash was not the result of an isolated problem with one or two companies such as Lehman Brothers or Bear Sterns. Instead, the subprime mess was a massive situation that was spread throughout the financial sector. That's why its collapse sent shockwaves that caused damage through virtually every sector in the entire stock market, and even the entire planet. Consequently, the world descended into a desperate financial situation that has not yet fully turned the corner. We are far from being out of the woods. That's why we call this systemic risk, since it affects the entire system.

In the subprime meltdown the S&P 500 index went from a high of about 1500 to plummet below 700.

When we compare the charts of BP and the S&P 500 Index, we see that we are still highly exposed and can easily lose half our investment to systemic risk (S&P 500) just like we can lose money to non-systemic risks (BP).

Looking back a bit further, the "dot-com" crash of 2000-2001 was centered in technology stocks. However, the problems also spread wider to the entire market. The 9/11 terrorist attacks helped accelerate the fall of a market that was overvalued by speculation in the first place.

Here's what this means to the average investor: You were told that the strategy of diversification was supposed to protect your retirement money. But the diversification common to 401(k)s offers nothing to protect investors from systemic crashes. Instead, it exposes all of your investments to large market drops.

When you suffer crushing blows to your account such as these market crashes, it can take decades to recover back to the point where you were. Suddenly, time becomes your worst enemy. Will there be enough time between now and when you dream of retiring not only to recapture your losses, but to grow your money to where it needs to be?

I believe that having an understanding of both non-systemic risk and systemic risk is essential before investing in any type of stock or other security. It is not enough to simply acknowledge that risk exists when we sign off on the fine print. Ideally, we should have a thorough understanding of what those risks are and how likely they are to actually happen. Most people will never take the time to understand what risks their investments face. That's why they were absolutely shocked when the Dow Jones Industrial Average tumbled from its height of 14,000 and decimated their retirement plans. They didn't see it coming. Perhaps they didn't even know it could happen like that. Ultimately, it didn't matter. They paid dearly for their ignorance, and will continue paying for a long time to come.

Know How to Talk the Talk

Investing is as much about communication as it is about money. Yet most people who are invested in these types of plans do not yet have the basic financial vocabulary to even communicate properly about the risks associated with their 401(k) plan. And most people who lost money in their plans don't even realize that they were victims of systemic risk. Chances are they understood the basic concept of diversification in hopes that winners would outnumber the occasional loser. But no one ever told them about the risks associated with that kind of diversification. As a result, they greatly overestimated the supposed safety of mutual funds.

Being a victim of systemic risk stems from not knowing the vocabulary that an investor needs to be successful. Because when it comes to investing, what you don't know can definitely hurt you. But when you know the language, and what those words mean, you will begin to gain more power and control over your future.

So why didn't your financial advisor tell you about systemic risk and make you aware of the fact that diversification does absolutely nothing to protect you against a systemic problem? Good question. Perhaps that's a question you should ask them.

Think of it from your financial advisor's perspective. If he told you that diversification doesn't really protect you against a systemic crash, how would that make his investment programs look? If you had known then what you know now, would you still have continued funneling your hard-earned money into his mutual funds?

Ultimately, you will need to look at the current situation of our economy and make a decision about what kinds of systemic risks are facing your investments.

The dot-com crash of 2000 is behind us, but ten years later the NASDAQ still had not made it back to the 5,000 level where it was before the crash. The subprime meltdown and associated crash is also in the past, but the investor cannot afford the long wait for the Dow Jones Average to hit its pre-crash high. But is the worst really behind us? How would you judge the systemic risk that is in today's environment? Are you still clinging to the same mutual funds in your 401(k) in the hope that the worst is over and that brighter days are to come? Do you think that the system will correct itself and produce returns that will outpace inflation in order to deliver a passive income that will allow us to live our dream retirement? If you look at where your 401(k) is today and where it needs to be at the time you wish to retire, does it look like smooth sailing or is it likely to need divine intervention to make it all happen?

A Measuring Stick for Risk

It's one thing to talk about risk, but another thing to measure that risk so we can understand it.

One of the ways I like to evaluate risk is to find out how much money it would cost to insure any specific kind of risk I'm interested in.

For example, suppose you have a teenage daughter who, by age 18, has already accumulated seven or eight speeding tickets. An insurance company may see her as a higher risk than your wife who has never had a single ticket. Because the teenager represents a larger risk, there's a strong likelihood that they will charge more money to insure your teenager than they will your wife. Insurance companies are experts at measuring and studying risk. They have actuarial tables, mathematical algorithms, and they run all kinds of possibilities and scenarios to make sure they are receiving enough premiums from enough people to cover the occasional claim. In my opinion, insurance companies understand risk better than anybody on the planet.

With that in mind, we can measure the amount of risk that exists in a given situation by determining how much money it would cost to insure that risk. To assess the health of a corporation you can learn to do what educated investors call a fundamental analysis. Fundamental analysis focuses on reading the financial statement of an entity and then determining if they are healthy or in trouble. It's a lot like getting a check-up at the doctor's office. But instead of taking a reading on blood pressure and other vital signs, fundamental analysis gives us a reading on cash-flow.

Using fundamental analysis to help us measure risk:

- A poor showing on a personal financial statement might put a family at risk of bankruptcy.
- A poor showing on a corporate financial statement might put a company at risk—and is seen as a non-systemic risk for investors.
- A poor showing on a government's financial statement might put an entire country's market at risk—and is a strong systemic risk for investors.

Government debt is also called *sovereign debt.* Most 401(k) investors don't pay attention to things such as the potential impact of the impending European sovereign debt crisis on their personal nest-egg of mutual funds. A brief discussion on sovereign debt will help you understand how insurance can be a measuring stick for risk.

Europe's Sovereign Debt Is Our Problem Too

Just as people have borrowed money to buy cars and houses, our governments have been borrowing money to pay for government programs promised by ambitious politicians. In the case of the United States, they borrow money for entitlement programs, defense, education, infrastructure, and other expenses. As a result, we are deeply in debt. The same story happened in Japan not too long ago. However, perhaps the most alarming situations are the immediate problems facing some of the European countries such as Greece, Portugal, Ireland, and Spain. The GDP of these countries does not allow for adequate taxation of their citizens to pay for the government programs they depend on. In other words, the government has given the citizens a drug habit they can't pay for.

So what does this have to do with insurance? Well, that's where something called credit default swaps come in. A credit default swap (CDS for short) is sort of like an insurance policy on sovereign debt. When the insurer feels that a nation could likely default on their debt, the more premium they will demand for the insurance. Recently, credit default swaps on European debt have hit an all-time high. This, of course, leads us to the question at hand: Exactly how much risk, especially systemic risk, exists in the world markets right now? If credit default swap prices are a measuring stick of systemic risk, then we are at an all-time high right now. Don't forget, diversification will not help in this type of situation.

Most people will ignore these warnings, and will continue to sleep comfortably listening to that lullaby of diversification. But that pleasant sleep will soon turn into a nightmare, because the weakness of sovereign financial statements around the world will most likely overpower anything Wall Street can do to try and prop up the economy.

Even as individual corporations look for ways to improve their balance sheets, I believe that the dire situations with sovereign debt will inflict massive systemic risk on all of us. In that setting, traditional 401(k) programs are not designed or equipped to protect you from such unprecedented systemic risks.

Will Japan's Situation Become Our Destiny?

In the 1980s Japan experienced a boom in housing prices very similar to the price escalation two decades later in the United States. Why did real estate prices rise so much? The short answer is because credit was easy to access, so people eagerly used that available credit to snap up properties. As a result, this huge demand pushed up prices to unsustainable levels.

During these real estate booms, everyone loves riding the wave of greed and excitement. But underneath these waves is a dangerous undertow that is ready to sweep careless investors out to sea. While most people are giddy about the boom, smart investors can look to common economic indicators to see what is really happening under the waves.

In the United States, one of the most popular economic indicators we look at is a stock market index called the S&P 500 Index. The S&P 500 index consists of 500 U.S. companies that are designed to represent the health of the overall stock market.

Similarly, Japan also has an index that helps investors gauge the performance of the Japanese markets. It's called the Nikkei 225 Index. So while Microsoft and Ford are companies that are members of the S&P 500, major Japanese companies such as electronics maker Sony and Japanese automaker Toyota are part of the Nikkei 225 Index.

In the late 1980s the Nikkei 225 Index soared from a level of about 10,000 in 1984 to an astounding height of nearly 39,000 in 1989. Then in 1990, the Japanese bubble burst and it all came tumbling down.

How did this happen? In hindsight, we can see that Japan implemented a monetary policy of quantitative easing and a fiscal policy of deficit spending. The result of these actions plunged Japan deeply into debt as it tried to recover from the crash.

Those two policies implemented by Japan are extremely noteworthy. When the Japanese government allowed large fiscal deficits combined with a monetary policy of increased currency supply, it caused Japan's debt to GDP ratio to soar. Here is why this is so important: The debt to GDP ratio is one of the most important numbers for us to look at when doing our fundamental analysis of a sovereign nation. The resulting number speaks volumes about the health of that nation's economic situation. GDP is essentially a country's economic engine from which taxes are collected. When a country's debt is allowed to become very large, then its GDP becomes insufficient to produce the taxes needed to pay the debt.

Policy Plus Demographics Equals the Future

The policy similarities between Japan of the 1980s and the United States of today is strikingly familiar. The United States Congress is the decision-making body which determines the country's fiscal policy. They have the responsibility of deciding how much revenue will be collected through taxes, and how much spending will be given to various government programs.

The Federal Reserve Board is the body which dictates the monetary policy of the country. At the time of this writing, their policy has been to increase the money supply and indulge in quantitative easing.

Much like Japan in the 1980s, the United States experienced a sharp housing boom from about 2002 up until the subprime lending meltdown of 2007/2008. The housing boom in the United States was caused by the same factors as the housing boom in Japan; buyers had easy access to money which created a huge demand for housing in a very short period of time.

Now that the housing market has collapsed in the United States, the Federal Reserve has adopted a similar policy that Japan chose to try and help their economic recovery, namely quantitative easing and increasing the money supply in the United States.

Let's look at how these actions will likely combine in the near future. In the United States, Congress has created a fiscal policy which currently promises citizens that reach a certain age entitlement benefits such as Social Security, Medicare, and Medicaid. When we examine the demographics of the baby boomer generation and apply the United States fiscal and monetary policies, the debt to GDP ratio the United States far surpasses that of what we saw in Japan nearly 30 years ago.

As of this writing, the debt to GDP ratio of Japan stands at about 235%, while in the United States it is about 100%. But when the baby boomers begin to retire en masse and become old enough to begin collecting their entitlement benefits, the debt to GDP ratio of the United States will skyrocket to around 350%. Compare that to what we are seeing in the news right now with the turmoil in Greece, and all the problems they are experiencing. Those problems are the result of a Greek debt to GDP ratio of about 140%. That is far less than what the United States will be facing in a short period of time.

Previously I showed you that the so-called 'diversification of mutual funds' does not protect us against systemic crashes. Because when the bottom drops from this impending bubble that is so similar to what Japan experienced, the entire market will fall with it.

Certainly there are differences between Japan and the United States. But there are enough similarities to provoke a smart investor into action. The first step should be to consult with our financial advisors concerning the systemic risk posed by the economic policies of United States.

Japan and the United States are similar in that they are two of the largest economies in the world. Both countries are advanced and enjoy similar standards of living. And most striking is that both countries have fiscal policies that incur massive deficit spending combined with monetary policies that are increasing the currency supply.

The difference is that Japan implemented these policies in a more prominent way much earlier than the United States has. If we're smart, we should be looking at what happened in Japan as an experiment of what those fiscal and monetary policies can do to a country's stock market, and thus the entire economy. Policy plus demographics gives us the future, which means the days ahead for the the United States could lead to a very sobering situation.

Diversification Didn't Help Japanese Investors

There are no guarantees in investing. It's impossible to say with complete certainty that the United States stock market will behave over the next 20 years just as the Japanese stock market has behaved over the last 20. But the economies, fiscal policies, and monetary policies are similar enough that we should be open to the possibility of this happening.

To help us understand what really happened in Japan, and what may happen in the United States, let's look at a chart of the Nikkei 225 Index from 1984 to 2011. In 1984, the Nikkei 225 Index was at nearly 10,000. As of this writing in 2011, the index is sitting around 8,600.

Show this chart to anyone who is trying to convince you to buy mutual funds and hold them for the next 25 years, and ask them this question: "If you knew the U.S. market would go this direction over the next quarter century, would you still encourage me to invest there?" As the United States finds itself in a frighteningly parallel situation to what Japan has experienced, you can see that it's entirely possible that the United States could experience a similar fate. While it's unknowable whether we will also experience nearly three decades of losses and stagnation, it only seems smart that we look at this situation with a clear mind and complete rationality.

Put yourself in the position of a Japanese investor. Imagine having a financial advisor back in the 1980s telling you to invest by diversifying throughout the Nikkei 225 Index to protect yourself. How would you feel if you had invested your retirement into that market when it was at about the 10,000 level in 1984 when you were at your prime age of 35, and now be staring at the Nikkei 225 Index at 8,300 when you would like to be ready for retirement at age 57?

What's the big lesson here? That systemic risk is real. Systemic risk is not some phantom bogeyman that never really materializes. Just ask the millions of Japanese investors who have been staring it down for nearly 30 years. When it comes to our retirement, we should be aware of every potential risk that stands in our way. When we know those risks, we can prepare to beat them. But when we invest in ignorance, we are setting ourselves up for failure.

The Case for the United States Is Grim

Perhaps the most qualified person in the world to speak on the systemic risk facing the United States is David Walker. Mr. Walker is the former Comptroller General of the United States and was the head of the Government Accountability Office for many years. Basically, he was the chief accountant of the government.

Mr. Walker understands the financial statement of the United States better than anyone. Although he is very articulate, when he speaks about our country's financial plight he seems to struggle to summon the language to appropriately convey the gravity he feels about the situation. He quit his job as Comptroller General out of utter frustration. His warnings to both Republicans and Democrats have been arrogantly ignored. So, like me, he has shifted his efforts away from appealing to legislators and placed his focus to educating individual citizens.

Search the Internet for "David Walker" to find more about his warnings for America. This isn't the ranting of a conspiracy theorist. This is a direct word of warning from the man who knows more about this country's financial situation than all of the politicians in Washington put together. He can teach you about budget deficits, trade deficits, leadership deficits, and education deficits. Walker's views are based on real numbers and not biased by a political agenda. He understands the real way to solve problems is through public education rather than legislation.

Systemic Crashes Will Keep You Working

The dot-com crash that had such a negative impact on the NASDAQ Composite Index is an example of just how long recovery can take. Ten years later…and the NASDAQ still had not been able to get back to its 5,000 pre-crash level. As of this writing the Dow Jones Industrial Average high of 14,000 is getting closer, but it still takes years to recover from a crash that happened over just a few months. Time is not a commodity that the baby boomer 401(k) investors have in abundance. It becomes more precious with every passing day. Which means that every time a systemic crash occurs it pushes that retirement date further and further into the future.

If it takes my retirement account 10 years to recover, what impact does that have on my life? If I was on track to retire at 65, now I'll need to continue working until I reach 75. That 10-year setback is serious. Even worse, we now live in a time where these 10-year setbacks can happen three or four times during our working years, if not more. And what happens if one of these crashes happens after we have already left our job for retirement? That kind of financial setback is brutal. It's also one of the reasons why I'm so passionate about spreading the message that 401(k)s are not what they're cracked up to be.

Timing the Market

Earlier I mentioned that the founder of Vanguard, John Bogle, has been very critical of the current state of the mutual fund industry as a whole concerning its conduct and values. He has also been very vocal in his stance against active investing or trading the markets. I'd have to agree that the majority of the people who might try market timing do not have the education or experience to benefit from short-term fluctuations in the market.

Yet I respectfully differ with Bogle and all those who promote the old-fashioned doctrine of buying into an index-following investment and holding it until we die. There is now simply just too much systemic risk in the world for this strategy to be a safe bet for the millions of investors who need a reliable return.

Here's an interesting way to look at this. The very people who preach against individual investors timing the market are at the same time asking us to time the market 30 years in advance. From that perspective, you have to wonder about their motives. In our modern world, think about how many things can occur during those 30 years: technology changes, political changes, environmental changes, and economic changes. The buy-and-hold strategy did work for some, up until several years ago. But that was a period of time before the creation of derivatives, hedge funds, and electronic trading that can cause "flash crashes" which can cut 10% from the Dow Jones Industrial Average during a single trading day.

Yet they still want us to believe that in today's environment the market can recover after a crash at a pace that can preserve our investment objectives. That's a dangerous and uncertain line of thinking. If the 401(k) was being used as a mere supplement to retirement income as it was originally intended, that may not be a completely bad approach. But with the near-total reliance on the 401(k) to supply retirement funds, it's hard to believe they keep singing that same song. When a person follows that brand of preaching, they are simply trading their non-systemic risk for massive systemic risk. And when it's your retirement at risk, there is just too much at stake for the buy-and-hold approach of 401(k)s to be useful.

Preparation vs. Prediction

As a final thought in this discussion of risk, I want to emphasize that much of risk, both systemic and non-systemic, can involve the element of surprise. The grim picture painted by sovereign fundamentals does not include the possibility of unexpected events. An example of this is the tragedy of 9/11. No one could have truly foreseen this event, nor the impact it has had on financial markets. That's why I teach that retirement investing needs to be more about preparing for the future than predicting the future. Systemic risk is real, prevalent, and has a high enough possibility of actually happening that it demands legitimate respect. The 401(k) plans do not offer any respect for systemic risk. Instead, they are waiting to be victims of it.

When defined pensions were the core of retirement income, we were able to more easily endure systemic risks. But the new risk introduced by a mass exodus from defined benefit pensions to contribution plans was largely unintentional. This is a perfect example of the law of unintended consequences.

Chapter Four

The Law of Unintended Consequences

Our world is filled with wonderful tools that help us get more done and make our lives more comfortable. Tools are all about solving problems. When we needed to keep our food cold so it wouldn't spoil so quickly, we developed the refrigerator. For more specialized tasks, such as pureeing vegetables, we created the food processor. We're surrounded by amazing tools, from the telephone to the washing machine to the personal computer.

If you want a problem solved correctly, you reach for the right tool.

But what happens when you use the wrong tool for the job? Imagine painting an entire house with a pastry brush. Or dusting your grandmother's knick-knacks with a chainsaw. If you try solving a specialized problem with the wrong tool, it can become a disaster.

That is exactly what has happened to our retirement system with 401(k)s, IRAs, and even Social Security. None of them were designed to shoulder the entire burden of income during retirement. They were designed to be supplementary to the income from traditional pensions for the worker, or passive income from assets acquired by the investor. Now these specialized tools are being sold to us to accomplish something that is virtually impossible. It's as if they are asking us to fill an Olympic-size swimming pool with a coffee mug.

Vitamins Are Not Complete Meals

We all know the value of taking a daily vitamin supplement. This little pill gives us the additional vitamins and minerals our body needs. But it was never intended to replace all of the proteins, carbohydrates, and fats our bodies require to be healthy.

Now let's think about what it takes to have a healthy personal financial statement. First of all, consider the income statement. If there is a positive cash flow—more income than expenses—then there are "nutrients" being fed to keep the financial body alive. But if the cash flow is negative—not enough income to cover expenses—it's like burning more calories than you take in. That's a good thing if you're trying to lose a little weight. But it's a bad thing when it comes to your financial health because it means you are either borrowing from your savings or taking on more debt to cover expenses.

If the savings in a 401(k) plan and Social Security payments are a person's only retirement income, it is like trying to live each day on only a vitamin pill and a glass of water. For many middle-class people, these two supplemental income sources won't even provide enough to cover basic expenses, let alone luxuries.

Understand What Congress Is Really Doing

It often seems as if the real-world results of the bills passed by Congress are exactly opposite to the titles they are given. Have you ever noticed that about new legislation? It would make a great comedy routine if this problem wasn't causing so much trouble.

The truth is that this buffoonery is truly a bi-partisan effort. Both conservatives and liberals are equally skilled at fooling the public with their antics.

For example, the Employee Retirement Income Security Act has become a death sentence for traditional retirement income from defined benefit plans.

Even worse was the legislation signed by President George W. Bush in 2006 called the "Pension Protection Act." Another shining example of the government standing up for the little guy, right? Wrong. In truth, this Act helped further destroy traditional pensions in favor of 401(k)s. It gave corporations the legal right to fleece their employees. We will talk more about this 900-page mess in a later chapter.

Ironically, legislation often does the exact opposite of its name, or what we're led to believe is its intention or goal. Someday we might learn that not everything can be done with legislation. Things like courage, goodness, hard work, responsibility, and financial education can't be placed in our brains through legislation.

Look closely and you'll see that even the names of our governmental institutions make no sense. The Federal Reserve Bank is not "federal" at all—it's a privately owned institution. Some say that it's not a real bank. And we all know it has no reserves.

Newton's Law of Legislation

Sir Isaac Newton was a very smart guy. He was able to notice what was happening in the world around him, and then develop mathematical descriptions of those events. One of the laws he described goes like this:

For every action, there is an equal and opposite reaction.

What this really means is that forces come in pairs. When a fish pushes its fins backward, it propels the fish forward. Powerful rocket engines push hot gases downward as the rocket goes shooting into the sky.

Harnessing these forces can do amazing things. However, if you don't consider that equal and opposite reaction when you take action, the results can be unexpected and even hazardous.

When Congress takes action by passing new laws, they typically do a poor job of forecasting what the equal and opposite reaction will be. In fact, my guess is that it rarely even becomes part of the debate. As a result of their good-intentioned but ultimately misguided efforts, it gives rise to the law of unintended consequences.

As citizens, these unintended consequences are then inflicted upon us to deal with.

An Unintended Consequence That Is Hurting You Right Now

Earlier I mentioned ERISA. Most people have no idea what it means. ERISA stands for Employee Retirement Income Security Act.

Remember what we said before? You can usually guess what a bill really does by taking the meaning that's the opposite of the title. This title, like those referenced earlier, is ironic because this law is largely responsible for pushing traditional pensions onto the endangered species list. Ultimately, it could lead to their total extinction.

To understand the unintended consequences of this particularly bad law, we need first to understand a little more about the two basic types of retirement plans that are present in today's financial arena.

Defined Benefit Plans

The defined benefit plan is a chapter in the evolution of the American dream from the opportunities and independence of 1776 to the entitlements and dependence of today.

Originally, the United States was a land that guaranteed life, liberty, and the pursuit of happiness—and not much else. That was all anyone really wanted. The price for that opportunity was a willingness to live in independence. There was no one to take care of you but yourself. There was no social security, no healthcare programs, and no government assistance of any kind. I'm no historian, but I picture this as a high risk, high reward environment. There were big winners and big losers.

Somewhere along the line people began to confuse the word freedom with equality. Being created as equals was not enough. The belief that all men are created equal began to be transformed into a culture with a new need to live as financial equals, rather than simply starting life as fiscal equals. We wanted more equality and less freedom. Today we see very few people teaching their kids that life is not fair, even though it isn't.

It took more than a hundred years for Social Security and other entitlement programs to come on the scene, but it started early on with a gradual shift from independence to dependence on the government and institutions. In a country whose most celebrated holiday is about independence, we have now reached a point where there are many people in the United States who are 100% dependent on programs like Social Security. The culture of dependence is beginning to engulf the country's traditional values of independence.

Long before the public became dependent on government and institutions, we became dependent on corporations. A college education became part of the American dream because a good job came with a good pension. For the individual, lofty ideals such as innovation, free enterprise, and entrepreneurship took a back seat. Instead, the average person's life work became focused more on competing for a job at a company that would pay you while you worked there and then continue to pay you a pension after you stopped working. These pension payments, given after working many years for a corporation, were not dependent on one's financial education, investments, or savings. They came from the resources of the company and came as a defined benefit until death. You did not outlive a defined pension. This was very attractive to people who felt more comfortable as workers than as investors or entrepreneurs. On the surface it appeared to be much less risky.

So a defined pension is retirement money that is paid by a company for the life of the employee. As you can imagine, these plans are very expensive. On the balance sheet, they are a liability to the company. This kind of a promise to pay workers after they retire is called a "legacy promise." The heavy burden of these legacy promises is one of the reasons why big corporations such as General Motors and United Airlines went bankrupt.

Now you can understand why these corporations are always looking for ways to reduce their expenses—especially when it comes to these legacy promises.

Contribution Plans

As the skyrocketing costs of legacy promises threatened the ability of these corporations to continue to exist, Congress stepped in and changed things in one fell swoop. By passing ERISA, they paved the way for new IRS tax code changes that were sold to the public as benefits to the average worker. Simply put, it gave workers a way to have their supplemental retirement money grow tax-deferred during their working years. This meant that taxes on those extra savings wouldn't be collected until the money was drawn out during retirement.

Virtually overnight, mutual fund companies had millions of potential new customers who needed an approved investment vehicle for these new retirement funds. The financial institutions that were selling mutual funds drooled at the treasure chest that was given to them. These new customers would receive a tax deduction by placing money in their funds, and were penalized if they withdrew it early. Congress essentially gave the mutual fund companies a captive audience.

Corporations were starry-eyed at the idea of not having to pay those expensive legacy promises that ensured a more reliable retirement for their workers. They loved the fact that now the huge burden for retirement could be taken off their shoulders and placed squarely on the shoulders of the workers. Based on our country's founding principles, that's not necessarily a bad thing. But there was a serious problem: These workers had no financial education.

Who could win in that scenario? We are the captive audience of mutual fund companies, and we know that Wall Street is winning big because of ERISA. Thanks to the rule changes that allowed corporations to drop the expensive defined benefit plans, these same big corporations also became big winners. Sadly, the loser is obvious—the worker.

This is a clear example of the law of unintended consequences. Congress probably had no idea that by passing ERISA, they were condemning millions of their fellow citizens to a retirement of shattered dreams. It would take a few decades to get there, but the evidence is growing every day. As I stated in Chapter One, 401(k)s are a result of Wall Street greed, not wise decision making.

Contribution plans require the worker to largely fund their own retirement by investing in financial instruments they simply don't understand. Worse yet, they do not give the person a reliable income until death like the defined benefit programs. On the contrary, when you have a 401(k) plan your income ends when the money is gone. Your ability to fund your entire retirement depends on many factors that are totally out of your control, such as market risk, inflation risk, longevity risk, and others. There is no other way to spin it—401(k) plans are a terrible deal for the worker.

Truth or Consequences

As we have seen, there are always consequences to an action. When someone makes an uninformed decision, there are often unintended consequences that can cause a lot of trouble.

The purpose of this chapter is to tell the hard truth so you will be aware of the consequences ahead of you. What started out as a small change to the U.S. tax code has now transformed the entire retirement future of America. Another unintended consequence has been the massive wealth handed over on a silver platter to the mutual fund companies who provide the investments for the 401(k) programs. On an even bigger scale, these types of programs have now spread to much of the world. It's an export we should be ashamed of.

Traditional pension programs are being phased out or just plain eliminated. During the 1990s, a landslide of major corporations made the shift away from traditional defined pensions to 401(k) plans. Not enough time has passed to prove that the 401(k) system works. So far, all evidence clearly shows that they are failing.

The Proof Is Overwhelming

Much of the remainder of this book will be spent explaining more of these unintended consequences caused by this shift to contribution retirement plans. It is shocking and alarming. But this information is vital to your future. You'll see the reasons why so many smart people detest the 401(k):

- They became the keystone of retirement instead of being supplementary.
- They made Wall Street rich instead of the investor.
- They have effectively killed traditional defined benefit plans.
- They have created artificial demand in the stock market and contributed to wealth-destroying bubbles.
- They will cause artificial supply in the market and cause massive crashes by way of mandatory distributions.
- They have placed uneducated investors in the driver's seat without knowing how to drive the car.

The list will continue to grow, because this isn't over. We may yet see many other problems that stem from ERISA. Unintended consequences have a way of popping up when you least expect them.

Use Your Head

We began this chapter discussing the value of using the right tool to fix the right problem. This applies not only to tools we create, but also to our minds. By gaining new information and learning new skills, we can transform our minds into specialized tools to solve unique problems. With this new information we can look at problems and make educated decisions. We don't have to be dependent on others. We can overcome knowledge gaps to become proficient at new things.

As the government continues to mess things up by making poor decisions, we can improve our own lives by countering with good decisions. It all comes down to developing the desire to overcome the things that have been holding us back. With the right training, we have the ability to become a better investor than we ever imagined. This is what freedom is all about: using our creativity and intelligence to set us free from the things that would otherwise hold us back.

Don't be alarmed. You may find you are better at learning new things than you ever imagined. After all, it's been proven that most people with a little knowledge can outperform the average mutual fund manager. With their sub-par performances over a long period of time, the bar has been set very low.

Chapter Five

The Savings Lie

In our culture we have a lot of sayings about the virtue of saving money… "Saving for a rainy day" … or "A penny saved is a penny earned." Saving is something we have valued for a long time.

When I was a boy I was given a piggy bank and taught the value of saving money. I was praised when I chose to drop my coins in the piggy bank instead of the gumball machine. When I was eight years old my father drove me to the bank and opened up a passbook savings account. I felt like a grownup. The practice of saving money has always been associated with wisdom, discipline, frugality, self control, and other desirable attributes.

Saving Money Has Been Hijacked

Imagine going to a friend's house to watch a big game. As you are enjoying the game and fun conversation, your friend passes you a can of your favorite brand of nuts to snack on. As you open the can, a fake, spring-loaded snake jumps out and startles you. Why does that gag work so well? It's because you trusted the label on the can. You thought it was your favorite brand, so you never saw it coming.

The huge institutions that reap billions from our 401(k) accounts have hijacked the term "saving money" and placed it on their can filled with mutual funds. They love to refer to 401(k) investments as "worker savings" or "saving for retirement" because of the positive emotional feeling we get from the term savings. People trust the concept of saving money. They feel good when they think they are putting money into their retirement account. Another way to look at it is with the term "a wolf in sheep's clothing." Because that's what a 401(k) account really is—a label you trust (savings) covering something you shouldn't (risky investments with no control). If you call a cow a dog, it doesn't really change anything because it's still a cow. They tell us that 401(k) accounts are worker savings plans, but they're really not. They are still risky investments.

By giving the 401(k) program the label of "saving money," it gives these firms an excuse when our account balances are low. In that situation, it's easy for them to place the blame on the saver instead of those getting paid handsomely for managing the money. After all, if your piggy bank is light, it's because you haven't filled it enough, right? So when all the indicators show that 401(k) balances will be grossly insufficient to sustain workers in retirement, the headlines read "Americans are not saving enough for retirement." In these moments the mutual fund industry has tricked everyone into believing it's not their fault. They have somehow given everyone amnesia because no one is talking about the mutual fund industry's favorite teachings: dollar cost averaging, the rule of 72, and the explosive growth that comes with compounding. The truth is, these sales lines have given the typical worker virtually no benefit in their 401(k) account. They sneakily shift the blame to you for not saving enough.

If we look past the label and open the can, we will find just how deceptive this hijacking really is. In today's world journalistic integrity has generally gone by the wayside. As the media has shifted its focus from factual reporting to sensationalism, they also get caught in the downward spiral of mislabeling events. As a result, formerly strong words like "crisis" have lost much of their bite due to overuse and inappropriate use in the news. They have been pressured by fierce competition to gain ratings in the world of 24-hour cable news. Now when any little event occurs, they quickly slap a label of crisis or emergency on it to try and get our attention. It's like the little boy who cried "wolf." With the entire 401(k) program facing serious problems in the near future, nobody is paying any attention. "Another crisis? Oh, they'll solve it tomorrow. I wonder what's happening in sports?"

High-level mutual fund industry insiders are the ones who truly understand that the coming fall of our retirement system is going to be a legitimate crisis. Let's look at another statement – this one from a 2006 interview for the PBS series *Frontline* titled 'Can You Afford to Retire?' – from Vanguard founder John Bogle because he says it better than anyone else:

> *"The whole retirement system, in fact, the country is in, I think, very poor shape, and it's going to be the next big financial crisis in the country, I honestly believe. We have a system that is troubled, and I don't see that our administration or our Congress is giving it the attention that it really has to have. I don't think anybody has a crisis kind of an attitude towards this. And if it's a crisis, I think it would help to have a crisis attitude."*

When will we be able to look past the mislabeling of 401(k) accounts and realize they are investments and not savings? Only then will we be ready to face the situation and deal with the issue of properly investing our retirement money so that it actually grows to our benefit—and not for the benefit of the financial institutions.

Earning Interest vs. Paying Fees

When I opened that first savings account at eight years old, I was taught about the benefits of saving money. First I was told that the money would be locked up safe and sound in a vault where no one would steal it. I was also taught that the bank would pay me some money called interest. If the interest rate on savings is low, you may not earn very much. But it's still a lot better than being charged all sorts of fees without getting good value in return. That's exactly what's happening to most retirement investors today.

If you put $10,000 in the bank your balance is $10,000. However, when you spend $10,000 on mutual funds you likely do not have $10,000 worth of mutual funds. Why? Many mutual funds have what is called a front-end "sales load." This is basically a sales charge that gives commissions to the brokerage that sells you the fund. The Financial Industry Regulatory

Authority (FINRA) allows for a sales load up to 8.5%. So if a mutual fund charges a front end sales load of 5.75%, your $10,000 is instantly dropped to $9,425 because of the $575 sales load. They take their first part of your money before they even lift a finger. In addition, back-end sales loads will take commission money when you sell your mutual funds to take a distribution.

Now you can see why it's incorrect to refer to these investment plans as a savings account. Because you aren't saving money, you are spending money on commissions and products.

What about No-Load Funds?

If you're not careful, it's easy to get hurt by the no-load label. For example getting a credit card with a label that says "0% introductory interest rate" sounds attractive, right? But if in the fine print there is a provision for the rate to jump to 19%, that card could easily cost you a lot of money if you don't watch the situation closely.

If a fund is advertised as a no-load fund, an educated investor might see that as a warning sign to be very cautious. They would carefully check the fine print for a myriad of other fees such as purchase fees, redemption fees, exchange fees, and account fees. None of these fees fall under the definition of a sales load, so the fund is legally correct in advertising they are a 0% no-load fund. Trust me, these financial institutions will not give you anything for free. They know how to get your money from you.

Fees Are Intentionally Hidden in the Chaos

When I explain these fees to people, this is one of the typical responses I hear: "Andy, I don't mind paying a little bit in fees in order to have them take care of my money." In principle, I totally support anyone who receives compensation by providing real value. As I show in this book, the value we get from these 401(k) companies is generally very poor. Yet they continue to find devious ways to take more and more from your account. And the worst part is trying to find all the fees your management company is charging. Many of these fees never even show up on your statement.

How chaotic is this whole situation? Here's a little insight that might make you dizzy trying to follow the convoluted path they have created:

> *A management fee goes toward the expenses of managing the fund except for the expenses that are incurred in managing the fund that don't count as management fees. Some fees are included in the expense ratio, and some are not. But don't confuse the net expense ratio with the prospectus expense ratio because they are not the same. Some fees you can avoid if you reinvest dividends back into the funds. Some are Class A, some are Class B, and so forth. There are fees for transaction costs and turnover. There are purchase fees that investors pay to buy the fund but are not categorized as sales loads because they are for the institution that created the fund and not the brokerage that sells it. Redemption fees are fees that you get hammered with when you take your money out, but are not the same as back-end loads because, like the purchase fee, this money is for the institution, not a commission to the brokerage, nor should this be confused with a contingent deferred sales load which obviously charges the investor more money if he wants his money back sooner than the mutual fund managers want to give it to him. Exchange fees cost you if you transfer to another fund within the same group. Account fees cost you if you fail to maintain a certain dollar amount in the account which are separate from other expenses that include shareholder service expenses; custodial expenses; legal expenses; accounting expenses; transfer agent expenses; and other administrative expenses that are not part of the management fees that we discussed earlier—except for when they are like the fee payable to the investment advisor which is different from the broker dealer.*

Were you able to follow that? If not, you shouldn't be surprised. It was created this way for a reason. They want it so confusing that you feel your only option is to grin and bear it. But it doesn't have to be that way.

The Arrogance Fee

In comparison, none of the fees mentioned above can hold a candle to the arrogance embodied in the 12b–1 fee. The 12b–1 is another fee charged to you as an investor in a fund. But what does the money generated from this go to? They are using your 12b–1 money to advertise the fund to new investors so they can collect more fees.

It's like going to the grocery store to buy milk and bread, and having a charge show up on your receipt that goes directly to help the store advertise on television and radio. Most businesses fund their marketing efforts from their overall revenue. But in the arrogant world of these financial institutions, they brazenly charge us this fee right out in the open.

Originally, the purpose of the 12b–1 fee was to help the funds grow large enough so they could eventually lower some of the other fees for their investors. Somewhere along the line, though, they became addicted to this free advertising money and forgot about reducing their other fees. Again, we are left with the bill.

Investing in Ignorance

Everyone has a place on The Education Continuum™:

Based on interviews I have with average people across the country, many who are invested in mutual funds do not know basic information about their investments, such as the expense ratio, let alone being familiar with the litany of fees they are paying and the rules tied to each fee. I believe the vast majority of 401(k) investors are currently at the ignorance end of the continuum.

Earlier I promised you that I wouldn't pull any punches in the discussion of this important topic. So I will tell you frankly that we have no business investing in things that we do not understand. Yet this is exactly what has happened to millions of investors across the country and around the world. We are enticed by good marketing to funnel our hard-earned money into investments that appear to be simple and safe. The truth is far different from this distorted vision.

Start with the Net Expense Ratio

Where is the best starting point for a typical 401(k) investor to begin understanding how much they are paying in fees? I recommend looking at the expense ratio as the first step. While not all fees charged by a fund are included in the expense ratio, it helps us understand some important things. First of all, the expense ratio is the amount of money the fund takes from you each year as payment to run the fund.

Knowing this kind of basic information is important if you are in a mutual fund. As you will see, fees are literally stealing the majority of your investment growth. In fact, if you track these fees over the life of your investments, the amounts piled up in the coffers of the institutions become so outrageously huge it will take your breath away. We will study how much they are actually taking in Chapter Nine.

Expense ratios typically range from .5% to 1% of the fund's assets, but some charge much more. This may not seem like much, but it actually has a huge impact on your results years down the road. It often adds up to billions for the mutual funds—even though many of them fail to outperform basic market benchmarks such as the S&P 500.

Seeing through the Smoke Screen

One of the most sadly amusing things to watch in the world of investing is the way mutual funds are compared to each other. In a sport like golf, it's easy to know who wins. At the end of a tournament, the golfer with the lowest number of strokes is the champion. At the end of the season, they count up the prize winnings of all the golfers across all the tournaments and declare the top money winner.

The mutual fund industry has a similar "award" system called the Lipper Indexes. Few have ever heard of this, but it's a big deal amongst the mutual fund companies. Essentially, the Lipper Indexes are a way for mutual funds to compare themselves against the average mutual fund. The resulting numbers are supposed to be helpful to investors as they seek the best performing funds. It's kind of like how the S&P 500 is an index of 500 different large cap stocks representing the total market so investors can see how their own investments are doing in comparison.

Lipper Indexes are similar in that they take a handful of mutual funds with similar objectives and create an index that represents the average of that category. Those numbers are then published for the public to see. Investors use the performance numbers to evaluate their funds and consider new ones. Mutual fund companies use the results as marketing ammunition. For example, it's common to see them boast that "our fund has beaten its Lipper average for five years in a row." But what does that really mean? If the entire category of mutual funds is outperforming the overall market, then the company has some substance behind its claim. Since most mutual funds do poorly compared to the broad market, however, what it usually means is that the "winning" fund is just the least terrible choice in that category. It's not actually a winner, it's just the least bad loser, if there is such a thing.

For example, in 2010 Lipper awarded the Evergreen Precious Metals Fund I (symbol: EKWAX) with the top spot as the Best Fund over 3 Years for Gold Oriented Funds . They even gave them a neat little certificate as proof of this grand achievement.

In addition, this EKWAX fund also received a coveted 4-Star rating from the Prestigious Morning Star rating service.

So what did EKWAX do to deserve such lofty praise? This fund invests in companies that deal with gold, such as mining companies. It does not directly invest in gold. At the first week of January 2008, EKWAX was at $71.76. Nearly three years later at the last week of December 2010, EKWAX was at $88.08. That's a gain of 22.74%.

Now let's compare that gain with what you would have earned had you simply invested directly in gold through the popular gold exchange traded fund (symbol: GLD). At the first week of January 2008, GLD was at $88.58. Again jumping forward nearly three years to the last week of December 2010, GLD was at $138.79. That results in a gain of 56.68%. In this case, a completely uneducated investor off the street could have invested in a gold correlated asset via the GLD exchange traded fund and would have earned 250% more than the expensive fund managers who handle the "winner" of the Lipper Index award.

In case you're wondering, EKWAX has about $1.53 billion in assets with a net expense ratio of 1.05%. Which means the fund takes about $16,065,000 of its investors' money each year to manage the money in the fund. To get into this fund, it will cost you a 5.75% max front-end load. So if you invest $10,000 in EKWAX you would actually start out with $9,425 because $575 has been sent to the guys who sold it to you as a commission. This is just one of the fees an investor should take into account when deciding if the expected yield and growth of the fund is a worthwhile investment. By comparison, that investor may look at the situation and simply decide to buy some gold.

Cash Withdrawals versus Selling Stock

Suppose it's payday and you have a nice check in your pocket made out to your name in the amount of $5,000. You go to the bank and deposit the check. A week later you need to withdraw $100, so you go the bank and ask for that amount. The teller quickly gives you your money. This is a basic example, but it shows something very important. When you take money from your bank account, the bank simply goes to its store of money and gives it to you.

However, when you withdraw money from an investment account such as a 401(k), your cash is likely tied up in a mutual fund and they have used the money to buy shares of stock. Remember, the company that manages your account has used your money to ultimately buy stock shares. In order to give everyone back their money, they must sell those shares in order to convert it into cash.

Furthermore, the amount you will receive from the sale of those stocks is based on the supply and demand in the stock market. If demand is low, they will have to sell more of the shares to give you the amount of money you want.

Remember, investing in mutual funds through a 401(k) plan is not the same as saving money. Your money is being used to purchase an inventory of stocks. When investors look at their 401(k) statement and see a dollar figure, they wrongly think of it as cash in the bank. When you understand that it's just a number representing the current value of the inventory of stocks you have purchased, it helps you realize the limitations and risks of the situation. Someday that inventory must be converted to cash by selling it. The price you will get for those stocks in the future is not guaranteed to be the price you can get today. It all depends on the mood of the buyers when that day comes for you. More on this in Chapter Eight.

Inflation Risk Versus Systemic risk

Saving money in today's world has become a much different action than simply putting a few coins in a jar. The nature of savings has changed because currency has changed. In 1971 the United States made saving money far more complicated when they changed our money system and moved away from the gold standard. At that moment the U.S. dollar became a fiat currency. It's not based on anything tangible. The Fed prefers to call it an "elastic currency." As a result, the U.S. dollar is now backed only by the government rather than by gold.

One of the risks of a fiat currency is that it seems a lot easier to print more money than to get your hands dirty and mine more gold. Maybe that's why the Federal Reserve invented terms such as "quantitative easing" or "monetizing the debt" or "expanding the balance sheet" to cover up when they want to print more money. However, the danger in printing more money is that it devalues the currency they are supposed to be helping. So it takes more notes to trade for goods and services, which is then reflected in higher prices. These across-the-board price increases are what we call inflation.

That's what makes saving money so much more complicated. If I save $10 in my piggy bank today, will it be worth the same a year from now? Perhaps that $10 will buy four loaves of bread today. If inflation rises and the cost of bread doubles, suddenly that $10 will only allow me to buy two loaves of bread. Thanks to the government's eagerness to print more money, they are causing my money to lose value.

So saving money carries with it the risk of inflation. That's different from the systemic risk that affects the mutual funds which are left vulnerable due to diversification, as we discussed in Chapter Three. Perhaps it's fortunate that a 401(k) is not a savings program due to the additional risk that inflation inflicts on our money system.

A Sports Car without an Engine

Imagine being given a brand new sports car. As you walk around it admiring the shiny paint, you can see yourself cornering perfectly on mountain switchbacks, and then opening it up on a long straightaway. This is a car designed to take you where you want to go.

You hop in the driver's seat and buckle yourself in tight. Running your hands over the steering wheel and gear shift knob, you can sense what the sudden acceleration will feel like. You reach for the key and turn it, but nothing happens. You try again. Still nothing. What's the matter? Isn't this car brand new? So you pop open the hood and suddenly your heart drops. The engine cavity is empty. You have a car that's all show and no go.

It's not too different from the way 401(k)s are sold to the workers in every type of company around the country. They want us to see the shiny paint and leather seats. They talk about how easy it is to use the "Rule of

72" to speed our way to riches. But when you look under the hood, you realize the same thing—there is no engine to power it.

That's because most 401(k) plans rely on mutual funds for their power. The problem is, mutual funds are bound to their limitations. There's no escape from these limitations, which inhibits their ability to get you where you want to go.

One of the financial reports I read on a regular basis is a quarterly report published by Standard & Poor's. It compares the performance of actively managed mutual funds against the indexes such as the well known S&P 500. Reading this report quarter after quarter is like listening to a broken record. Time and time again the majority of mutual funds failed to beat the index over long time periods. Which means that in order to perform better than a mutual fund, all I had to do was switch off my brain and put my money in an index fund.

The Mutual Fund Track Record

It's extremely important to remember that mutual funds are products. Products need to be sold. Therefore, it is up to us—the buyers—to beware of the salesmanship and tactics used by the mutual fund companies to persuade us to buy their products.

Just like a car salesman, the mutual fund companies will talk about the sexy parts of the car such as the shiny paint, the leather seats, and the great gas mileage. They don't want you to bog them down asking about how the engine works. And they definitely don't want you to get into the details of whether or not the system is set up to really help you win.

Luxury Price, Clunker Performance

We can point to the crash of 2008 as an example of the dangers of systemic risk. Like most investments, mutual funds were hit hard during that time. But when you look further back before the 2008 crash, we can see that mutual funds deliver questionable results in light of the billions of dollars they earn in fees.

One of the most well-known funds in the world is the Fidelity Magellan mutual fund made famous by fund manager Peter Lynch. (Side note: Peter Lynch famously claimed that an educated individual investor can outperform 95% of mutual fund managers. I tend to agree.)

From 1995 to 2008, the Fidelity Magellan Fund alone reaped $4.8 billion in fees for the company. Yet during that thirteen-year time frame, Fidelity Magellan grossly underperformed against the S&P 500.

How can it possibly cost $4.8 billion dollars to manage a fund? More importantly, how can $4.8 billion dollars worth of financial management produce such stunningly below average results?

It is not uncommon to see actively managed funds underperform the market averages.

But Fidelity is not alone. They get attention because they are well known and high profile. When you look at mutual funds as a group—even when you disregard the 2008 crash—you will still find that the results are consistently below average and nowhere near where you would expect them to be compared to the massive amounts of fees generated for the management companies.

In the first quarter of 2007, before the subprime crash, Standard & Poor's reported that the majority of actively managed mutual funds failed to beat their corresponding benchmarks. They found that over the previous five years the S&P 500 had beaten 72.2% of large-cap funds, the S&P MidCap 400 had outperformed 77.4% of mid-cap funds, and the S&P SmallCap 600 had outpaced 77.7% of small-cap funds.

Billions of dollars in fees were spent on poor investing performance before 2008, only to see years of hard-earned money disappear in the 2008 meltdown.

Many economists pointed to 2010 as perhaps the beginning of the much-hoped-for market recovery. Have mutual funds shown improvements since that time? Sadly, the answer is no. Well over half of the actively managed funds still underperformed their benchmarks in the 2010 S&P mid-year report. Over the previous five years the S&P 500 had beaten 61.83% of large-cap funds, the S&P MidCap 400 had outperformed 78.19% of mid-cap funds, and the S&P SmallCap 600 had outpaced 63.02% of small-cap funds.

The actively managed growth funds fared even worse, with 82% of those funds failing to outperform the S&P 500 growth index.

No Consistency Means No Compounding

One of the sales pitches used to persuade us to buy into the mutual fund mindset is the power of compounding over time. However, compounding is only beneficial when the rates of return are consistently high enough to cause your money to grow.

So when we look at individual funds to determine whether their returns are consistent enough to grow our money in a meaningful way, the results are just as disheartening. The data, pulled from Research Insights from S&P Indices, shows that the top performing funds rarely stay on top for very long.

Of the funds with a top half ranking in 2004:

- Only 4.27% of actively managed large-cap funds maintained their top half ranking in 2009.
- Only 3.98% of actively managed mid-cap funds maintained their top half ranking in 2009.

- Only 9.13% of actively managed small-cap funds maintained their top half ranking in 2009.

If we look at the top quartile performers, the top 25%, over the same period, the consistency is even worse. No large-cap or mid-cap funds, and only one small-cap fund maintained a top quartile ranking over the same period.

This suggests the disclaimer they offer is actually quite prophetic: Past performance really is not an indication of future results.

Actual Results Are the Goal

There are two ways you can measure the return of a mutual fund: relative and actual. Actual return is the amount gained or lost during a period of time. Relative return is what we have just been discussing, the performance against a benchmark like the S&P 500.

It's useful for us to use relative numbers to get a better idea of how investments are performing overall. But the truth of the matter is that we need our investments to give us strong *actual* returns. Otherwise, the investment is a failure. That's why it's not good enough to simply have your investments outperform the S&P 500. Because if the S&P 500 has lost half its value, how can we be happy if we only lose 45% of our money? In that situation, there is no good news in beating the market average.

An investment should have a goal to achieve. For a retirement account, that goal should be to provide us with enough passive income in the retirement years to live as comfortably as we desire. If our 401(k) accounts are not helping us get to that goal, there is something seriously wrong. We need strong actual returns, not empty promises.

You Ain't Seen Nothin' Yet

Despite the poor results, the growth of mutual funds continues to explode both in the United States and around the world. According to the

Investment Company Institute, mutual fund assets worldwide increased 10.5% to $23.70 trillion at the end of the third quarter 2010. Multiply that by even a conservative expense ratio and you can see how the massive amount of money at stake surely gets the greed glands of every investment company working at full capacity. It's no surprise that more and more companies want a piece of that pie, too. In the same report, the ICI stated the number of mutual funds worldwide stood at 68,863 at the end of the third quarter 2010.

With that kind of horrible track record, how do mutual funds attract so much money?

I think one of the ways is because of the sales pitch they use. They appeal to our common sense that there's no such thing as getting rich quick. So they turn it on its head and convince us that with their help we can get rich slowly. Kind of like the tortoise and the hare act; slow and steady wins the race. All they really do is perform a little brainwashing on us so we're not angry when we get our performance statements. Instead of getting mad, the little voice inside us says, "Don't worry, it's all part of the plan. Next month will be better. Besides, now we can buy more shares at a lower price!"

Unfortunately, that little voice they have trained is totally wrong. For many 401(k) owners, slow and steady has put them even further behind and moved the finish line out another hundred miles. That's a lot of ground for a tortoise to make up... probably too much.

Mutual fund companies also entice us with the "power of compounding." They sell the idea of compounding as if it were a supercharger for their engine. There's certainly no denying the math behind compound interest. It's very powerful stuff. Just one problem: Compounding only works in your favor when the rate of return is reliable. In the case of the stock market, the rate is extremely variable and often negative. What then? If the value of your account drops by 50%, you suddenly find yourself in a position where you need the market to jump up by 100% just to get you back where you were before.

This is just another unintended consequence of the whole 401(k) system. Employees are given crippled investment vehicles to try and reach their retirement finish line. If you decide to stay in that car, you'll be pushing it a long way home.

The next time you read a headline that says "Americans are not saving enough money for retirement," just remember that the mutual fund industry has hijacked the "saving money" label and slapped it on their sneaky little can filled with mutual funds

When examined side-by-side the difference is like night and day:

With a savings account...	With a 401(k)...
You make a deposit	You make a purchase
You have cash	You have an inventory
You earn interest	You pay fees
There is inflation risk	This is market risk
You make a withdrawal	You need a buyer

One problem with trying to save your way to retirement or participate in a 401(k) is that you have precious little control over so many vital factors. It is foolish to leave something as important as your retirement to a wish. It's even more dangerous to equate the word "hope" with the word "wish."

Chapter Six

The 401(k) Wishing Well

Back in one of my high school math classes I first discovered the magic of compound interest. As I worked the story problems about compound interest, I remember my surprise at the answers I arrived at. The numbers seemed too big. So I did the math again and again. Eventually I realized that time and interest are really like growing bacteria in a Petri dish. It grows fast!

Now that I'm neck-deep in everyday life, those story problems aren't just boring numbers. I can understand how each part of an investment is a living, breathing thing with its own personality. I like to think of the three variables as three brothers: Money, Rate, and Time.

Money is the brother that gets all the attention. He is like an overrated quarterback who never admits that his success is really all thanks to his good offensive line. He is overconfident and attractive. Every girl wants to be his date for the prom. In reality, though, Money is the least important brother in the family. Why? Because he is overrated and replaceable.

Rate is the bookworm brother. His value to the family is due to his education and financial intelligence. He is also tireless, working 24/7/365 with endless energy. Rate is the catalyst that transfers wealth from one party to another.

The last brother, Time, is the cypher. He's mute. He is also terminally ill and slowly dying. Unlike his brother, Money, there is no way to replace him. Unlike his brother, Rate, all the study in the world cannot improve his condition or extend his life. Most of the time he goes unnoticed because he never cries out for attention. On that rare occasion when he is noticed, we see his condition has grown progressively worse. He is always becoming more anemic, malnourished, and is withering away before our eyes.

Looking at this family of brothers gives us an improved view of compounding:

- A person can start compounding with very little money.
- A person can improve their rate of return with financial education.
- But a person cannot do anything to get more time.

Time stands alone and moves along regardless of one's personal agenda. We must work within Time's demands, because it will not bend to our will. Time is constant. It cannot be manufactured or replaced. Today the sun will set and another day will die.

The concept of time decay is very profound. It means that Rate must do his work right now without delay. It means that there is no such thing as deathbed repentance for the investor. Now is the time for Rate to perform its labor.

Set the Date

Every March I play in a fun, local basketball tournament. It's a different brand of March Madness because my body is now a long way from where it was in college. I know that Icy Hot and ibuprofen can only go so far. So about the first week of December I set a weight loss goal for myself in order to be ready to play.

At a rate of two pounds a week, I can lose about twenty pounds before that tournament. But if I go off the nutrition and exercise plan for a while, it becomes nearly impossible to reach my goal. There simply isn't enough time. I must stick to my plan because time will run out at some point. I can't buy more time. The same is true with your retirement plan.

My plan to prepare for a basketball tournament is not that much different from a retirement plan. It has an objective that is very specific. It has a schedule of progress. It has a date on the calendar for completion.

Most of us lack a specific plan. We seem to think that a retirement plan is just an account labeled "retirement."

For me, knowing the exact day my tournament begins is vital for me because it helps me structure a plan that is achievable. I can make a plan where reaching success is both probable and likely.

Without a detailed plan at the beginning, it's difficult to get where you want to be. And 401(k)s are as ambiguous as they come. They are not about creating a plan where you can mark your progress as you head toward your goal. Instead, all they offer is a "take what you get" approach. You can't control the results, you can only accept whatever happens—good or bad.

Here's what I want you to do. Get on a computer and open up a calendar that lets you schedule things in the future. Go to the date you want to retire and schedule it. It might be next year, or it might be in 30 years. Whenever it is for you, mark it right now. Be specific about that day of the week, even the time of day when you want to retire. Know for sure that that day, and that moment, will come. It is inevitable: That day will come.

Now make a shopping list for your dream life. Be sure to account for big price increases due to inflation. Account for first class seats. Account for the country club membership. Account for service to your community or church. Make a list with prices and get details on costs. Tally the cost of your retirement and enter that number on the calendar.

Now look at you retirement plan today in comparison to where it needs to be. Then choose which of the following words best describes your plan.

Your Plan: Likely, Hopeful, or Impossible?

A goal is a waste of time if it is not likely that it can be achieved. The best plans are ones where you have a high degree of control to ensure that the goal is met. For example setting a goal to win the lottery is not really a goal at all—it's just a wish. Because you have no control over the lottery results, it needs to be placed in the "hopeful" category. Sure, winning the lottery is a possibility, but it's not likely to happen. If I really want to win the lottery, the only plan I can have is to play it each day and hope.

As I speak to large groups around the country, I think this is the situation many people find themselves in when it comes to their retirement investing plan. They hope the market will help them retire, but they have no control over the situation. They cannot force the market to move up, and they cannot prevent it from falling. It is a plan based purely on hope and nothing else.

I am a firm believer in the law of the harvest, because I believe that you truly do reap what you sow. You receive what you plan for. It's an old saying from the world of farming. Let's look at two types of farmers to help us understand the principle of control a little better.

First there is the dry farmer. He plants his crops and hopes it will rain to help them grow. He does not have any contingency plan if it doesn't rain. He has not installed any kind of irrigation system in case the rain never comes. He is limited in the crops he can plant just as the uneducated investor has a limit to what investments are suitable for him.

Next, there is the irrigation farmer. He doesn't trust the skies to bring him rain. Maybe he's been around long enough to realize that if he wants to make money next harvest season he needs to take matters into his own hands. That's why he has set up all of his fields with irrigation to make sure the crops are well watered. He leaves nothing to chance.

This simple illustration shows us how risk is related to control.

- More Control = Less Risk
- Less Control = More Risk
- No Control = Ultimate Risk (gambling)

The irrigation farmer is not guaranteed a harvest, but because he has taken control of the situation, his success is much more likely to happen.

The dry farmer hopes for a harvest, but he has less control because of his decision to not irrigate. He is now dependent on the skies to smile on him by bringing rain.

Finally, there is a third person who does not plant anything at all. What will happen to him? He will starve because his plan is not possible.

If you don't put seeds in the ground, there is no chance food will grow. He needs a miracle.

So the question is, where do you stand right now? Is your current plan likely to succeed? Or does it fall in the category of hopeful? Or is retirement simply not possible on your current path?

Food for Thought

Now let's take a look at a scenario that's a little closer to home. It might feel a little bit familiar to you.

For the sake of this example, let's suppose that the Dow Jones Industrial Average is at the 10,000 level. And let's also suppose that your 401(k) account currently stands at $100,000.

If you are like most people, you have probably noticed that this account balance usually fluctuates right in step with the overall market. (Not to beat a dead horse, but I again call into question the effectiveness and intelligence of a financial advisor who ties your retirement to the unpredictability of the market!) If this is what is happening to your account, you can easily see that the market is what really determines your fate more than your financial advisor.

Suppose that your goal is for this retirement account to grow to $1,000,000 when you reach retirement age. And let's also suppose you are a baby boomer with about 10 more years to go before that retirement date arrives. Which means your account must grow 10-fold during that time. Remember, your success is tied to the market. So the question before you is this: How likely is it that the Dow Jones average will skyrocket to the 100,000 level by the time you retire? Because under your current plan, that is the only way your account will reach the financial goal you have set.

Is it possible it could happen? Yes.

Is it likely to happen? I'll let you answer that for yourself.

Aim for the Likely

Your life does not belong to someone else. Your goals are set by you to achieve what you want. That's why something as important as your financial situation in retirement should steer clear of simply hoping it will happen. If it is truly important to you, your retirement plan should be firmly in the "likely" category. However, the truth is grim: many middle-class 401(k) investors are in the hopeful or impossible category.

We cannot force the market to go up, and we cannot stop it from falling again. Even if the market goes up a little, most people need it to go up higher and faster than is likely with our economic situation. For many, winning the race is becoming virtually impossible.

Throwing Wrenches into the Gears

From the foundation of our country through 1971, the United States monetary system was backed by the amount of precious metals we had locked up in the US Treasury. Every coin or paper note the government issued was a symbol for the equivalent amount of silver or gold that it represented. Under that system, our money had meaning.

But in 1971 under Richard Nixon, the government decided that it was time to move away from such an old-fashioned idea. They moved us to a new system where the government could print as much money as it wanted without the need of having gold and silver in the bank to back it up. As mentioned earlier, we now have a fiat currency—meaning a currency with no intrinsic value. So for the past 40 years, the U.S. dollar isn't worth any amount of precious metal. It's only worth what the world thinks it is worth. And that estimate of worth is at risk of going down now more than ever before.

Switching to a fiat currency may very well prove to be the downfall of the entire U.S. economy.

Much of our nation's money policy comes from the Federal Reserve. They attempt to maintain some degree of control over the economy as they try to keep it humming along. One of their most potent and feared powers is called Quantitative Easing (QE). Basically, it means they print more money out of thin air to pump into the economy. How do they do this? In essence they write a check to buy Treasury Bonds even though they don't have the money to back the check—they create it out of thin air.

QE is so powerful and unpredictable that they only pull it out of their bag of tricks as a last resort. If the economy is stagnant or falling, and nothing else is working to improve it, they will sometimes try a little QE therapy to see if it can help.

As a therapy, QE is not for the faint of heart. It comes with serious side-effects that can sometimes be worse than the disease it is treating. So if lowering interest rates doesn't work to heat up the economy, then the Federal Reserve will print up more money to try and help the situation. But what are those nasty QE side effects? Just a little something called inflation. Because when you add more money to the system, you dilute the value of every dollar. So the makers and sellers of goods will increase their prices to get the value they need.

At this point you may be asking yourself this question: "So what?"

Well, here's what it means to the average person. Even if the Dow skyrockets to 100,000 to put a million dollars in your 401(k) account, suddenly you have a new problem staring you in the face. Your original plan for that million dollars was to finance a very nice retirement. But because of inflation, now all of those nice things you wanted cost a lot more than you ever imagined. Your wealth has been stolen by inflation.

The mutual funds that make up the bulk of 401(k) investments generally grow very slowly. No one has ever accused mutual funds of growing their clients' money too fast. When inflation starts growing faster, the 401(k) now places you in another unstable situation. Not only is it unlikely you will ever hit your original financial goal, but now it can barely stay ahead of inflation. It's like trying to catch a runaway freight train in a golf cart.

It all goes back to underestimating the power of giving away control of your future. None of us have control over what the Fed does with

Quantitative Easing. But as we see them taking these unwise steps, we can likewise make wise decisions to counteract them.

Currency Is Not Wealth

What is currency? When we were kids, we are taught that currency is money. Everyone loves having a fat wallet loaded with currency.

But currency is just another way to hold wealth. And it has its own set of risks.

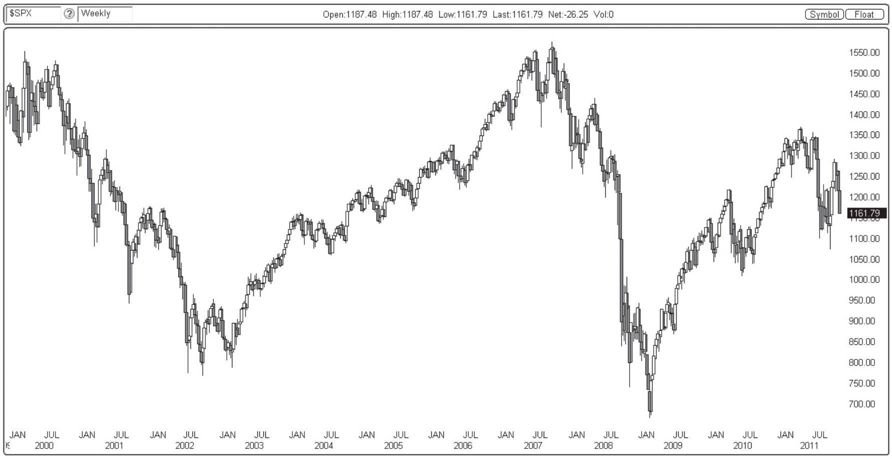
Imagine you have $6 to invest. Where is the best place to put that money? After doing a little investigating, you narrow down your choices. You decide to put $3 into a gallon of gasoline, and the other $3 into the bank. How fast will your investments grow?

After a period of time, you look at your bank statement and see that your $3 has grown to $3.10. At that same point, you see that the price of gasoline has also increased to $6.20. What does this mean? It means that your bank investment has lost half of its wealth.

It might sound far-fetched, but that is exactly what is happening to us today. As we sit and watch our 401(k) plans growing at a snail's pace, the price of the goods and services we will need to sustain us continue to rise all around us. We might think that money in our bank accounts represents wealth that is safe and secure, but in many cases it actually represents a loss of wealth compared to the prices we must pay.

What about Reverse?

Not only does a 401(k) put your money into the slow lane, it may even unexpectedly throw you into reverse. There are plenty of precedents that prove it happens frequently. After all, we just completed what is now known as the Decade of Nothing. The average investor basically lost an entire decade with no growth.



Remember the three brothers? It's bad enough when Rate takes a vacation. But when he starts to work against you by giving you a negative return, it puts you in a serious predicament. Losing ground with a poor investment tool such as a 401(k) is difficult to overcome because the math is cold and unforgiving. That is one of the prices that must be paid when control is handed over to someone else.

One Step Back Requires Two Steps Forward

At the end of the last chapter I mentioned this situation, but I want to explain it a little more fully to ensure you completely understand the seriousness of market losses.

Suppose you have $100 invested in the stock market. One day, the market experiences a big drop and your investment is now at just $50. You have just experienced a 50% loss. In this situation, how much do you need the market to increase to get back to where you were? The market will need to grow by 100% before you can break even. We know those kinds of increases can take time. The market is unlikely to double overnight. While you are waiting, a lot of precious time is being eaten up.

In the real world, we keep waiting for the Dow to get back to 14,000. When it does, it's not a signal that everything is going great. All it means is that you have recovered what you previously lost to the market. Brother Money is having his photo taken again at the prom, while Brother Time is home sick in bed, getting ever closer to his expiration date.

For people who went from age 55 to 65 with their retirement money in 401(k)s during the Decade of Nothing, there is nothing to celebrate. Now is the time to let Brother Rate work for you in a smart, pre-planned way. When you put him to work the right way, he takes no vacations, he won't sabotage your growth, and won't throw you into reverse.

You Can't Afford to Hope

There is no shame in looking at your current retirement plan and realizing it is based on fleeting hope. Because it's not our fault. We were sold a poor product based on lies.

However, if you do find yourself in this situation, please know that you do have a choice. You can take back control of your future. Remember, hope is what we stand on when we have no control. You might not be able to do much about how much money you have right now. You cannot get back lost time. What's done is done and it's water under the bridge. But you can seek a better rate for your investments to help it compound more in your favor. With sufficient financial education the future is yours to create.

I hope it's becoming clear why I started this book with the theme of financial education. Brother Rate is who you want on your side to help you. We know he gets stronger with more financial education and understanding. As I look around my own circle of influence, those who receive the highest rates of return on their investments are the people with the most financial education. And they didn't learn it in public schools or at a university. They took the initiative on their own.

This book is really an invitation to you to set education goals that will help you achieve your money and lifestyle goals. When you think of successful investors you will be convinced that education is the solution to move retirement goals from "hopeful" to "likely."

Those who are selling mutual funds will likely disagree with the idea that an average person can improve the rates they earn on their investments. That's fine with me, because this book is not written for them. It's written for anyone who is feeling crushed by our bad retirement system. It's for those of us who at one point bought into the false vision taught by the mutual fund industry. It's for those who are not willing to risk another 10 years hoping that it all turns out okay. Because if nothing changes, it probably won't.

Chapter Seven

The Power of Special Interest

We've talked a little about the benefits of compound interest. At this point, it's time for us to look at the overwhelming power of special interest.

What is special interest? Special interest groups are people outside the government who use their influence to put pressure on elected officials to advance the agenda of their group.

One of the great truths of this world is that big money equals big power. And big power means big influence. When Congress gets together to make decisions about new laws and changes to old laws, how do they decide what issues need to be discussed? Many times, they listen to the people who have helped them get elected. Or they listen to the people who helped them get a great deal on the mortgage for their new home. Or the ones who helped their spouse get a high-paying position. After getting help like this, of course they would want to help their friends, right?

Laws are then created to give advantages to these groups that know how to use their influence. Anyone who does not believe this happens every day in the corridors of any government building needs to wake up and smell the coffee. The wealthy elite in the financial industry has been exerting its power on government as far back as we can see. It is happening today, and it will certainly happen in the future. As long as there is money at stake, there will always be special interest pushing its own agenda.

Take the Federal Reserve Bank for example. The Federal Reserve Act was pushed through congress on December 23, 1913. The chief architect of the act was Nelson W. Aldrich. Aldrich's daughter was married to John

D. Rockefeller Jr. He was also a colleague of business magnate J.P. Morgan. Through relationships such as this, government has always felt pressure from the financial industry elite to create legislation in their best interest.

When Congress passed ERISA in 1974, they handed the mutual fund companies massive wealth on a silver platter. ERISA was the gateway to tax-deferred retirement plans. Today, workers are lured by tax incentives to buy mutual funds from the financial industry. The workers are on autopilot as they unthinkingly feed their 401(k) plans. With the help of this government-approved system, the financial industry skims a portion of each paycheck year in and year out as mutual fund companies rake in billions of dollars in fees regardless of the performance of the mutual funds.

Do you think the mutual fund companies will let that just go away? Or will they fight to get even more of a stranglehold to ensure that money will always continue coming into their overflowing coffers? We already know the answer to that one. President Bush signed the Pension Protection Act in 2006 that gave even more power to these financial institutions.

It doesn't take much effort to see how wrong-minded our legislators can be. If they see a problem, their first instinct is to pass a new law to try and fix it. As we have shown, the law of unintended consequences is rarely considered. And you and I are usually the ones who have to deal with these problems until they get so bad that Congress is forced to try and figure out another solution.

Please remember to check your political party affiliation at the door when we discuss these issues. In the United States, this problem is bigger than Democrats and Republicans. In fact, both parties are equal offenders when it comes to giving preferential treatment to special interest groups. Both parties have unknowingly conspired to put us at serious retirement risk. As investors, our responsibility is to learn how to play this game instead of figuring out how to change it. There are powerful forces conspiring against us. We need to outthink and outmaneuver them so we can win.

The Rot Beneath the Surface

In an ideal world, Congress would pass laws to serve and help the people. Who knows? Maybe some of the elected officials even care about us. The truth is, however, that many laws are passed to help special interest groups gain even more wealth and power.

How does this work? Let's take a closer look at President Bush's Pension Protection Act of 2006 to see how the financial industry's special interest power has skillfully used Congress. I want to show you how they have masterfully set up a plan that is fully endorsed by the government to essentially turn all of us into money-making sheep they can fleece year after year from the moment we get our first job to the moment we die.

Sound far-fetched? I'll let you make that judgment after you better understand what really happened on that fateful day.

Before we study this law, let's try to put ourselves inside the boardroom of a special interest group to see how we might try and manipulate laws to serve our business. One way to do this is to get a law passed that gives consumers a tax break if they spend their money with us. That's one of the proven tricks used by Congress. To get people to spend money on something, give them a tax break.

Suppose we have a business that sells motor sports equipment such as snow machines, jet skis, and motorcycles. Business is down, so we want to find a way to sell more machines. After a lot of digging, we find an obscure university study that might be able to help us. The study shows that people who are able to blow off steam when they are away from work are actually more productive when they go back on the job.

With this little study in hand, we start thinking: maybe the entire country's GDP could increase if all the workers simply had more fun on the weekends? Then perhaps we find another study that shows how families that play together develop stronger relationships and family values. The study also shows that in these stronger families, the risk of teenagers getting pregnant is cut in half.

Now the wheels are really turning in our heads. If we can just get more people playing on our machines every weekend, our nation will be a much better place, right? Workers will be more productive and GDP will go up. Teenage pregnancy rates drop like a rock, saving us billions in welfare. So we take this sales message to Congress: "Look at the benefits to the country! The good stuff goes up, and the bad stuff goes down. It's a win-win for everyone! We need to make this happen fast. So let's give a tax deduction to everyone that buys a sports machine." Basically, we have done the politician's job for them. We give them the "facts" they can use on the floor of the legislature to push their new righteous cause. Families will be strengthened, babies will be saved, and America will be restored to its former glory. And a few months later, a law is passed giving us exactly what we wanted in the beginning.

It all started with a selfish need to sell more machines. Then money and influence were used to make it happen.

Instead of snow machines, what if we were selling mutual funds? When you look closely at that Pension Protection Act of 2006, the power of this massive special interest group can be seen quite clearly. As Jeanne Sahadi for CNN Money reported in 2006:

> *"The new legislation encourages companies to automatically enroll 401(k)-eligible employees and to automatically increase worker contributions every year. It also allows the plan provider chosen by the employer to offer investment advice to workers.*
>
> *"Automatic enrollment is expected to boost the participation rate in 401(k) plans beyond 90 %."*

This law gives the average employer incentives to not just offer a 401(k) plan to its employees, but to automatically sign them up for a 401(k) unless they specifically say no. In other words, when an employee starts a new job the employer can push them into a 401(k) and automatically take money from each paycheck to buy mutual funds. The mutual fund companies will make money before the paycheck even hits the employee's bank account.

It gets better. This law also allows the amount of funds taken from the paycheck to be increased automatically each year. Plus, it also allows the company managing the 401(k) account to contact the employee and offer them personal "financial advice" to sign them up for even more financial products.

A casual observer might think it's a good thing to help employees build their retirement account as early as possible. But we know that it has very little to do with helping the individual and everything to do with boosting the ever-growing power and influence of the mutual fund companies.

We can only imagine how the mutual fund companies pulled it off. But the results of their efforts are clear. What company in the world wouldn't want virtually everyone to be placed in a program to automatically buy their products? With that kind of money at stake, most corporations would do everything in their power to make it happen. And because this law was passed, we know that some of them did take the necessary action to get it in place.

Now we have this Pension Protection Act of 2006 placed in the law books. It is happening all over the country. Congress gave a little tax break carrot for companies to enroll their employees. Mutual funds strengthened their grip on the average worker. And here's the best part: This whole thing was sold to us with this message that "Americans are not putting enough away for retirement. This law will help people save more."

The mutual fund industry has sold us the idea that participation in 401(k) plans is a good thing for the worker. But higher participation rates actually equal greater assets under management for the financial industry. Passing a law that is designed to increase participation rates is passing a law that makes mutual fund companies more money. When we understand that fact, we realize that it is not even subtle.

Section 902 of the Pension Protection Act is filled with a whirlwind of cross-referencing legalese that epitomizes the chaos that give rise to the title of this book. What is absolutely clear is that the law is overtly designed to get more people to automatically buy financial products before they even see their paycheck.

of 1986 and section 204(j)(7) of the Employee Retirement Income Security Act of 1974 (as added by this section) to employer securities to which this paragraph applies, the applicable percentage shall be determined without regard to this paragraph.

SEC. 902. INCREASING PARTICIPATION THROUGH AUTOMATIC CONTRIBUTION ARRANGEMENTS.

(a) IN GENERAL.—Section 401(k) of the Internal Revenue Code of 1986 (relating to cash or deferred arrangement) is amended by adding at the end the following new paragraph:

"(13) ALTERNATIVE METHOD FOR AUTOMATIC CONTRIBUTION

That final insult is the icing on the cake. The mutual fund companies got exactly what they wanted by putting the blame on us. They use the "savings lie" to claim that Americans are not saving enough for retirement.

The U.S. Department of Labor offers literature to business owners to further facilitate this automatic enrollment. Apparently it's not enough to just pass the law to send money to the mutual fund companies. They have also figured out a way to our taxpayer dollars to print their advertising as well.

Savvy business owners are always concerned about liability. Imagine automatically taking part of your employees' money and placing it into the stock market. Then imagine that the person you hire to invest that money loses it in risky stocks. That scenario has all the makings of a lawsuit, right? Oddly enough, the Department of Labor teaches business owners that they are absolved of this responsibility. Which means that it's completely okay for them to implement these automatic enrollment programs.

Here is an excerpt from a brochure distributed by the Department of Labor titled, *Automatic Enrollment 401(k) Plans for Small Businesses.*

> *"The fiduciary responsibilities cover the process used to carry out the plan functions rather than simply the end results. For example, if you or someone you hire makes the investment decisions for the plan, an investment does not have to be a "winner" if it was part of a prudent overall diversified investment portfolio for the plan."*

In other words, business owners need not worry if their employees lose their retirement to systemic risk. The law is focused on the means instead of the ends. Who cares if you lose your retirement money as long as you were diversified?

The very fact that they take such great pains to absolve themselves of having to deliver results should tell us that they are acutely aware of the risk and do not want to assume any of it. The risk is placed squarely on the shoulders of the worker.

The financial industry has convinced us that diversification is "prudent" and that exposing workers' retirement money—a lifetime of work—to systemic risk is an acceptable practice. It bears repeating that most workers have little or no financial education and simply trust their employer and their financial industry to take care of them. They often have no understating of terms like "systemic risk" and are utterly oblivious to the fees they pay for their mutual funds.

Privatized Social Security

You probably already know the Social Security system is heading for a meltdown. Congress stole all the reserves from this system many years ago. There are some that are calling it a Ponzi scheme. Ponzi scheme or not, the fact remains that it has now failed to stay afloat. Social security is now insolvent. We just passed the tipping point where more money is going out than is coming in, which puts our entire financial system under tremendous pressure because of the legacy promises that have been made to fund people during their retirement.

Never missing the scent of blood, the financial industry of course stepped up to the plate to offer their expert services. I can just imagine the conversation over lunch in their executive dining room: "I've got an idea. You know how Social Security is on its deathbed? How about if we convince the government to give us all the Social Security money coming in and we'll manage it for them. Then we'll pull off our percentage of those billions of dollars every year. Do you think we can get them to do it?"

Of course they can. And they probably will.

We have been hearing rumblings about this for a long time. Some politicians will surely test the waters to see how viable it is with polling numbers. Why not? By helping the special interests who helped them get elected, the politicians will be helping to solidify their positions. And if it can be sold to the public as salvation for the floundering Social Security system, then they will have another opportunity for plenty of back-slapping and hand-shaking as they have yet again "saved America." It will look just like the signing ceremony for the Pension Protection Act.

You will see politicians begin to speak of legislation that allows the rising generation to "opt out" of Social Security. Remember, when corporations could no longer afford to pay for defined benefit pensions, the financial industry stood by licking their chops to take over the employees' retirement accounts by selling them mutual funds. Now that the government is unable to pay for Social Security, the financial industry is salivating again. With no financial education to assist in making smart decisions, opting out of Social Security is like jumping out of the frying pan and into the fire.

Where Did the Investors Go?

In the midst of all this, what has happened to the idea of being a real investor? Not someone who puts blind trust in a system that is working against them, but a real investor who is educated on sound fundamental and technical principles to make wise decisions. An investor who rejects boilerplate investing because he can see through the flimsy salesmanship of the mutual funds. One that can take advantage of the market in any situation—either up or down—because she has multiple cash flow strategies in her arsenal. One who understands how to hedge risk and can use leverage to protect an investment rather than to speculate on it. What happened to that idea? The term investor is losing its meaning as we continue to be told that it's too specialized and difficult to learn. But now we know the truth about why they want to keep us in the dark.

Remember, there is a difference between having some investments and being an investor.

Chapter Eight

The Prophesy

One of my greatest mentors is Robert Kiyosaki. Among the many books he has written, perhaps my favorite is one titled *Rich Dad's Prophecy*. I highly recommend it, because it is a message of warning and urgency for those who want to know the truth.

In this chapter I want to touch on a few of the prophecies from Robert Kiyosaki's book and how they relate to our discussion about 401(k)s and mutual funds.

The concept of "inventory" is one of the most powerful lessons I want to teach in this book. A few chapters ago I mentioned the fact that many people think that wealth means they have a lot of currency. This is an incorrect assumption. Remember, we have many options where we can place our wealth. Currency is just one of those options.

Cash is only a medium of exchange. It makes it easy when we want to acquire something. For a seller, it is much easier to place a price of $10 on a pair of sunglasses than to negotiate with each buyer how many sandwiches you will trade for, or how many socks, or even bus tokens. Cash streamlines that process for us.

But that view of cash can also cloud our vision about what cash means to us. For example, an investor might look at their 401(k) statement and see that it has a current value of $250,000. In their minds, they can envision that amount of money in there just like a bank account. But that isn't the reality of the situation. Here's why: When you place money in a bank, you are giving it to them for safekeeping. We have to remember that the mutual fund industry uses the term "worker savings" as a label to place on their can filled with mutual funds. Banks provide a commitment to give you that money whenever you need it. However, your 401(k) fund is very different. Because your account doesn't have money, it only has shares of mutual funds. Which means that if you ever want to withdraw money from your 401(k), you must ask to liquidate your shares into currency.

In other words, your 401(k) does not have money in it. It only has an inventory of mutual fund shares that only have value to you when they are sold in the open marketplace.

The Curse of Inventory

Years ago I was a partner in a business that sold machines and parts for those machines. I was a silent partner, and so the managing partner was the guy really running the business. One day we were having our regular meeting where the managing partner reported back to us about the health of the company. During that meeting I learned that the inventory levels in our parts department had grown to more than $1 million. My stomach dropped when I heard the news, because I knew we were in trouble.

The problem was that the million dollars was not wealth for us. It was all sitting there in machine parts. These parts get old as new machine models are created. They just sit there and do nothing. And the only way to get cash from those parts is to find a buyer for them, which depends on supply and demand. I instantly realized that our ability to transform those parts back into cash was totally out of our control. Because we had given up control of the situation through buying a million dollars worth of parts, our risk of losing skyrocketed. Remember: less control equals more risk, and more control equals less risk.

The Law of Supply and Demand

The concept of supply and demand exists anywhere there is someone who has something that another person wants. It's especially strong in the stock market. Unlike my parts inventory, the stock market is much more liquid, which means that it's easier to find a buyer for your stocks than it is to find buyers of machine parts. But when you have high liquidity, you also have high volatility. Volatility is represented by those crazy stock price swings that can go up big one day and down the next. Flash crashes can happen in the market because of the market's high liquidity.

If you were at retirement age and decided to begin pulling money from your 401(k) today, what would be the effect on the market? Since you are just one person with a relatively small number of mutual fund holdings, this transaction would barely register a blip.

But we're just starting the period of time when a massive number of baby boomers are hitting retirement age. What happens when a million people start putting their shares up for sale? Or ten million, or fifty million? In that situation, the market will be flooded with sellers trying to liquidate their mutual funds. Try to visualize all the baby boomers trying to turn their mutual funds into cash at the same time. According to the law of supply and demand, when there is far more supply than demand, prices plummet.

We have literally millions and millions of baby boomers who will be forced by the government to begin selling some of their mutual fund shares at the same time. Yes, you read that correctly. Every 401(k) owner will be subject to mandatory distributions when they come of age.

Governments love mandates such as this because it gives them control over the people and forces them to buy or sell certain goods and services. In my personal interaction with the investors I meet, I have found that the majority of 401(k) participants are unaware of this mandate. They don't even realize their own government will force them to move their wealth out of the equity markets.

This glut of inventory will push the value of these shares down. So if a share is worth $25 today but its value in the near future gets pushed down to $15 during this massive sell-off, you have just lost 40% of your wealth.

And what was the cause of this avalanche-sized problem bearing down on us? It was that fateful law passed back in 1974; ERISA's unintended consequences are about to hit us.

In the last chapter we talked about how lawmakers will often entice us to do certain things with financial incentives such as tax breaks. On the other hand, they can also pass laws that force us to do other things. One interesting aspect of ERISA is that it does both. It encourages us to buy through tax break incentives, and then forces us to sell at certain times.

Although we are given a tax break when we put the money into the 401(k), and it is allowed to grow tax-deferred, at some point the government will want their share of that money through tax. That's why they added that part to ERISA that forces us to begin liquidating when we reach retirement age. They demand that tax revenue from us.

The Magic Number is 70.5

In the United States, the age at which the government forces us to begin taking money from our 401(k) plans for taxation is 70½. You can begin taking distributions and take the tax hit as soon as age 59½. However, you will be forced to begin at age 70½.

Millions of baby boomers will be hitting that age at about the same time, and the law will now force them to pull their money. As we discussed, taking money out of your account isn't like taking money from the bank. The mutual fund company must sell some of their holdings to generate cash for you. Estimates are that the size of this baby boomer surge is 70-80 million people hitting that age at about the same time. By law, they must sell some of their mutual funds for cash to pay the taxes demanded by the government.

In order to sell, you need someone on the other end who wants to buy. This whole precarious system is built on the hope that the next generation will buy these shares when the baby boomers need them to. But there are two major problems working against that happening. First of all, Generation X and Y do not have the money to buy up all these investments—especially at current market values. And, even if they did have some money available to invest, there are far more baby boomers with money than there are young people. Either way you look at it, there is a huge shortage of buyers who can snap up these shares when the boomers begin selling in droves.

This doesn't even account for the people who will be selling in order to get money to live on. Nor does it account for the need to sell to pay for rising healthcare costs. And it definitely doesn't count the people who will start bailing out of their investments as quickly as possible when the market begins to slide again.

Will the New Generation Bail Us Out?

Back in the 1930s, our nation went through the Great Depression. Right on the heels of that came World War II. Because of the real economic hardships that came from those time periods, people treated their resources with utmost respect. This was especially true about money. The generation that came from this time period became savers. Back then it made sense to save, because, as we have discussed, the currency system was entirely different.

However, when the nation moved to a fiat currency in 1971 saving money began to lose its value and didn't make as much sense anymore. Since money no longer had intrinsic value, many people realized it was wiser to move their money to other places than a bank.

In addition, the generations after World War II experienced abundance at levels never seen before. As a result, living the good life truly became a way of life. These younger generations stopped saving the way their parents did, because they thought the good life would never end.

- WWII Generation: earned money and saved it.
- Baby Boomers: earned money and spent it.

Even though baby boomers didn't save a lot of money, they still paid cash for things. As newlyweds they had secondhand dining room furniture and lived in small one-bedroom apartments. They got by with what they had.

Now, with Generation X, we have a new generation that has been focused on enjoying the very best of life as quickly as possible. As newlyweds they are buying big homes filled with top-notch furniture and big-screen televisions. They drive high-end cars and wear designer clothes. They strive to look successful before they actually become successful. However, since their income is not yet high enough to pay cash for these nice things, how do they pay for it? The financial industry has made it easy for them with credit cards.

- WWII Generation: earned money and saved it.
- Baby Boomers: earned money and spent it.
- Generation X: spends money they don't have, and are now trying to earn it.

The problem with the exploding debt held by Generation X isn't just their problem. It's everybody's problem. Their focus is going to be on paying for that debt they have acquired. One of the last things on their mind is investing for their own future. The present is hard enough for them. So how can we expect them to have enough money to buy the investments their parents are trying to offload? They simply don't have the resources to absorb this avalanche of selling that is coming their way.

What about China?

China's rise as an economic powerhouse has been an amazing story to watch. And it continues to unfold. Part of China's financial and political strategy has been to buy a lot of the U.S. government's debt. But will they also be there to buy when the baby boomers need to sell the mutual funds from their 401(k)s?

Think about it and see if you can guess what China will do in this situation. Armed with the knowledge you now have about this impending sell-off, would you buy when the prices are at their highest? Or would you wait until it hits rock-bottom to get valuable assets at a discount?

Looking at it from that perspective, it's easier to understand how other nations with the power to help will probably sit on the sidelines and wait for the bargains.

It's important to remember that this broader economic outlook is just one issue related to the 401(k) fiasco. But when you add it to everything else we are discovering about this retirement plan that has been transformed into the monster we are now dealing with, it becomes very serious indeed. Yet most people have no clue that they are caught in the middle of this brewing storm.

In fact, you are in the minority if you knew beforehand that mandatory distribution from a 401(k) occurs at age 70½. The general public is largely unaware of the laws related to their 401(k) plan and how those laws affect them. And that's just the way the big financial firms want it.

The Storm Could Come Sooner than Later

Every investor should have a basic understanding of the debt market and the equities market. Debt means we have given someone a loan and they have promised to pay us back with interest. Equity is ownership with the hope that what we own increases in value, or pays a dividend, or both.

Traditionally, if there are any assets remaining when a company goes bankrupt, the bondholders get their share of any money left before the stockholders. This is one reason why bonds (debt) are generally considered to be less risky than stocks (equity).And the potential rewards associated with each of these reflect their respective risk.

As people age, they run shorter and shorter on time. Recoveries from a crash can take a lot of that precious time to get back to where they started. That long recovery period can make holding money in equities much riskier than holding money in debt. Thus, financial advisors often decrease positions in the equity markets and increase positions in the debt market as people age. Simply put, they sell stocks and buy bonds. There is an argument that a sell-off in equity mutual funds could be possible far before that 70½ age line in the sand is reached. So much for boilerplate investing.

Automatic 401(k) enrollment and boilerplate investing encourage investing ignorance. We are seduced into believing that someone smarter than us is in charge. We are tricked into believing they are interested in doing the right thing for us. Unfortunately, that is not how capitalists operate.

Chapter Nine

Stealth Wealth

In earlier chapters you began to see how the mutual fund fees you are charged through your 401(k) plan make it very clear that this is not a savings plan. It's a buying plan.

In this chapter we are going to look again at the issue of mutual fund fees in a more in-depth way. This explanation of how fees are charged and what it means to your retirement nest-egg is perhaps the most important part of this entire book. Please follow along closely to be sure you understand the concept of how mutual funds are keeping the bulk of your investment earnings for themselves. You may even need to read this chapter two or three times to fully comprehend what is happening to your money.

Over the course of this explanation we are going to bundle up all of the different fees charged to mutual fund investors so we can explain what they mean to the average investor who places his trust in the 401(k) system. As we walk through this process, we will also decode how this legal robbery is jeopardizing our future well-being during retirement.

Please be forewarned: This is not a discussion for the faint of heart. When I walk people through this process so they understand the devastation these fees are inflicting on their nest-egg, emotions often rise to a boiling point. I have had audiences ready to grab pitchforks and torches to storm Wall Street because of this information I am about to reveal to you. That is why this chapter comes with a warning. Because once you learn this new knowledge, you cannot unlearn it. Your new understanding will always be there when you open those quarterly 401(k) statements and imagine what the size of your account could be compared to what the numbers on the paper are telling you. Perhaps you will never consider investing without a solid financial education when you begin to understand how the system really works.

Before we jump into the details of this chapter, I also want to make it clear that the explanations in this chapter do not come from my own opinion or creative thinking. Everything you are about to read reflects explanations from some of the most influential and trusted professionals in the financial industry. These men have revealed the bare facts regarding the consequences that fees impose on the average 401(k) investor. Again, these words are not my own. These industry leaders have publicly spoken them. My goal is to simply convey them in such a way that more people can hear and understand this important message to help them make wise decisions about their own money.

The Price Is NOT Right

There is a popular television game show where they choose audience guests to participate onstage in various games for a chance to win prizes. Most of the games they play involve the guest's ability to know the typical retail price of different consumer goods. It's interesting to watch the show and see how well-dialed-in these guests are to prices. The win rate seems to be very high when it comes to knowing the price of a box of laundry detergent, a frozen pizza, or even a new car.

I wonder what would happen, though, if they asked some questions about their retirement investments.

> *How much are you paying in management fees for the mutual funds in your 401(k)?*
>
> *What fees are they legally allowed to hide from you?*
>
> *Are you paying a 12b-1 fee? And if so, how much?*

My guess is that virtually no one would win prizes, since so few know the answers to those questions. Plus, it's not the kind of stuff that makes a fun television show.

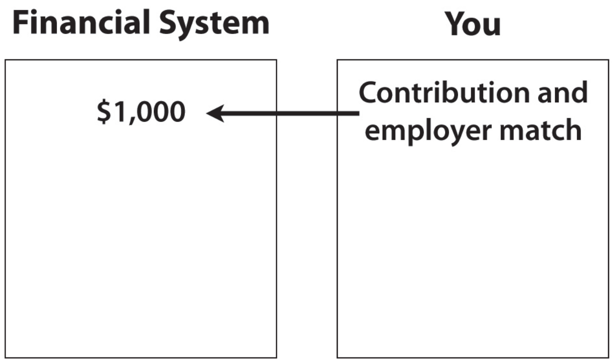
But I think you get the point. If we use common sense in our everyday lives, we have to ask ourselves whether or not it makes sense to purchase a product or service with no idea how much is costs. We are very good at knowing how much we spend on our cell phone bill. We know our house payment. We will even drive a couple extra blocks to save three cents a gallon for gas. But most people have no clue what they pay for money management. Is this being financially smart or financially silly? If we don't know how much this financial advice is costing us, then how can we compare the value we receive compared to the fees we pay? If we don't know how much these companies charge, how can we keep them in check? Giving your money to Wall Street with no concern over fees is like asking a fox to watch over the hen house without keeping count of your chickens.

But as we saw in Chapter Five, that information simply is not on our radar screens. When they sold us on investing in our 401(k) plan, they never taught us how to keep score. Do you think that is a coincidence, or is it by design?

By keeping us in the dark about what we are really paying for their services, the financial institutions are able to bring in huge profits without any outrage from their customers. They have created a system that is like a stealth fighter. It works at high speed doing its job with vicious efficiency without attracting any negative attention.

Most of us are on autopilot when it comes to participating in our retirement investing. We just dump money from every paycheck into the 401(k) imagining that it is a smart move because our employer offers an "employer match." On the surface it looks good because it seems as if we are getting free money, right? But this money isn't given to us. It is added to our account that is under the control of the management company. It becomes part of what financial institutions call "assets under management." Those matching funds are now subject to all the fees that the management company extracts.

Now let's take a look at what Wall Street does with our account funds so we can see how much we can expect to get back in our retirement years. It's helpful to track our money as it is exchanged back and forth from us to the management company using simple illustrations of the process.



John Bogle Revisited

As I mentioned in the beginning of this chapter, we will let respected financial industry insiders tell us how these fees affect our retirement earnings. First, let's learn from John Bogle, founder and former CEO of the Vanguard Group. Mr. Bogle is one of the pioneers of the entire mutual fund industry and is still actively involved in the mutual fund debate. When I teach about 401(k)s, I often refer to the following example given by Mr. Bogle because it helps us understand what is happening with our money in the mutual fund system from one of the men who helped develop this entire industry.

In 2006, John Bogle was interviewed by PBS for their *Frontline* series. It was a documentary on retirement, and I highly recommend you watch it if you get the chance.

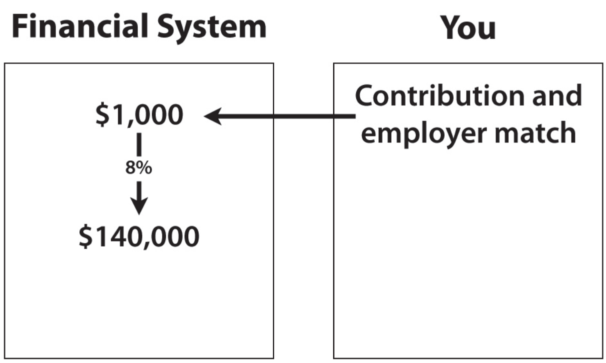
During the interview, Mr. Bogle was asked a question we all should have asked ourselves long before we put a dime of our retirement money in the hands of the financial institutions:

"What percentage of my net growth is going to fees in a 401(k) plan?"

As you carefully read Bogle's response to this important question, we will illustrate his explanation with diagrams.

> *"Well, it's awesome. Let me give you a little longer-term example. The example I use in my book is an individual who is 20 years old today starting to accumulate for retirement. That person has about 45 years to go before retirement -- 20 to 65 -- and then, if you believe the actuarial tables, another 20 years to go before death mercifully brings his or her life to a close. So that's 65 years of investing. If you invest $1,000 at the beginning of that time and earn 8%, that $1,000 will grow in that 65-year period to around $140,000."*

In the illustration below of Bogle's example, we see that a one-time investment of $1,000 at a steady rate of return can grow into a large amount of money.



The magic of compound interest makes this money grow like magic. Many financial advisors use the truths of compounding growth to entice us into giving them our money to manage. And the truth is that compounding does work, There is no trickery in the math. The trickery comes in the fact that this compounding benefits the institution and not us. Let's continue following Mr. Bogle's example:

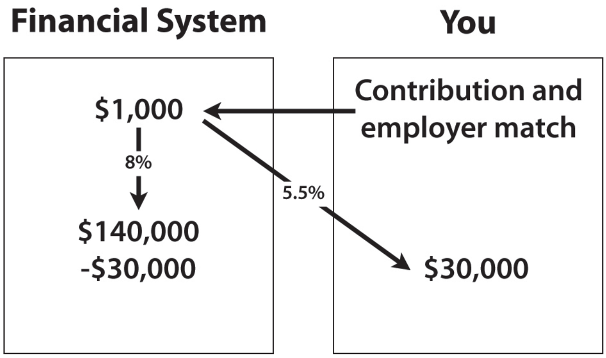
"Now, the financial system—the mutual fund system in this case—will take about 2½ percentage points out of that return. So you will have a gross return of 8%, a net return of 5.5%, and your $1,000 will grow to approximately $30,000."

Did you see what happened? How can there be such a massive difference between what our account earns and what we actually get back from the mutual fund company? The key is the seemingly small 2.5% they take for themselves. It doesn't look like a lot, does it? But this is what happens when we reduce our rate of compounding by that 2.5%. If the rest of the scenario plays out and our money earns an average of 8% over those 45 years, then our account can indeed compound to $140,000. All of that growth occurs while the money is in the hands of the management company, and they always take their cut before it flows through to our account. What this means to you is that your investment in this scenario is actually only growing at 5.5%.

The difference between an investment that grows at 8% and one that grows at 5.5% is massive. How can an investment account earning a smaller rate reach your retirement goals? The only way to do it is to hold that investment even longer. But with retirement inching closer every day, the possibility of that happening becomes increasingly unrealistic.

I am always shocked when people tell me they don't believe they pay 2.5% in management fees. What many of these good people fail to understand is that some fees are in plain sight while others are hidden away in the chaos, as I explained earlier. Some people even take it very personally when I discuss it with them. One gentleman boasted to me that he did not pay any hidden fees. When I asked him how he knew this, he quickly answered, "Because I've never seen any."

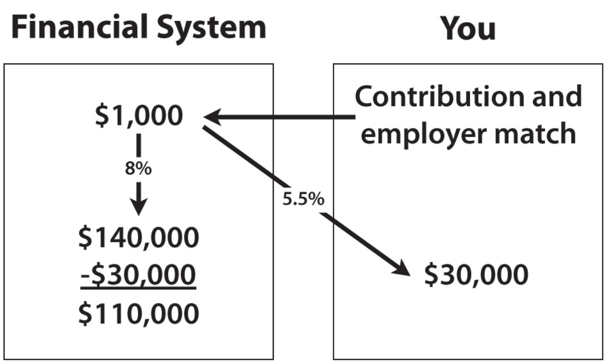
Let's look at what is happening with our initial $1,000 that has compounded at 8% to $140,000, and yet the amount reflected in our account has only grown to $30,000 because it only compounded at 5.5%:



This is what John Bogle refers to as the "tyranny" of compounding costs. Compounding does work—but in this case, it works in favor of Wall Street instead of the investor. Mr. Bogle continues:

"One hundred ten thousand dollars goes to the financial system and $30,000 to you, the investor. Think about that."

Yes, let's do think about that and ask another question: *What's wrong with this picture?*



When you ask people how much they pay in fees on $1,000 they typically have no clue. They might say 1% or 2%. It sounds like a very small amount, right? "What's the big deal, it's only a few bucks." But when compounded over the long term it eats up the vast majority of your profits.

In most scenarios this would be seen as criminal theft. But since it's on Wall Street, this robbing of your henhouse is 100% legal.

The Perfect Money Machine: Infinite Return with No Risk

The tyranny of these compounding fees is the fuel that runs this perfect money machine created by Wall Street. John Bogle continues:

> *"That means the financial system puts up zero percent of the capital and took zero percent of the risk and got almost 80% of the return, and you, the investor in this long time period, an investment lifetime, put up 100% of the capital, took 100% of the risk, and got only a little bit over 20% of the return."*

I am not mathematician and I don't like making things complex. I like things that are simple. But in this case, your entire well-being in retirement relies on understanding a little basic math. When you understand how this one equation works, you will understand why this is the perfect money machine for these financial institutions.

We are going to use a very simple calculation called arithmetic return. This is how investors determine the percentage return they receive on an investment. To calculate arithmetic return, you only need two numbers:

1. The initial value of the investment
2. The final value of the investment

Step one is to subtract the initial value of the investment from the final value. Step two is to divide that difference by the initial investment. In math form it looks like this:

$$\frac{\text{(final value)} - \text{(initial value)}}{\text{(initial value)}}$$

Here's a simple example to show you how it works. Suppose you bought a stock for $100 (the initial value) and today you are selling it for $110 (the final value). To calculate the return we take the final value of the investment (which is $110) and subtract its initial value of $100, giving us a difference of $10. Now we divide that difference by the initial value of $100 to get a return of 10%.

$$\frac{(\$110) - (\$100)}{(\$100)} = 10\%$$

Now let's calculate the return percentage for the financial institutions on our 401(k) accounts. Since this is your money and not theirs, their initial investment is zero. In our example, their final value is $110,000. So let's do the math:

$$\frac{(\$110{,}000) - (\$0)}{(\$0)} = \infty\%$$

Yes, you are seeing that correctly. When the initial investment is zero the arithmetic return becomes infinite. Dividing by zero makes for a number so big that it is undefined. Your mutual fund management company is earning an infinite return on your money while you shoulder 100% of the risk burden.

What is frustrating for so many investors is that they would not mind paying for an investment management service that is worth the money. Good advice from trained professionals is extremely valuable. I gladly pay accountants and attorneys for their services that are difficult for me to do on my own and provide tremendous value. When I use these professionals correctly, they improve my bottom line.

By contrast, a system that sends the majority of the profits to the advisors is just plain wrong—even if it is legal. This point is underscored in light of the facts showing how most of these mutual fund managers fail to outperform the market.

How much intellectual prowess is required to simply follow the market?

What am I paying tens of thousands of dollars for?

Is it worth giving the majority of the growth away just to be diversified?

Does is seem right at the end of the day that the longer I leave my money with them the more compounding costs work ***against*** *me?*

What about protection? If I can still lose my money in a system-wide crash, then what protection does professional management really give me?

When these companies manage our money and skim a part of our profits, it is the perfect business scenario. There is no manufacturing, no shipping, and no inventory. They simply collect their portion of the money every year. What is their secret? They teach us to buy and hold. They teach us that dollar cost averaging is a smart strategy. They teach us that we're not smart enough to manage our own investments. They will tell us anything they can think of to keep us pumping money into their coffers every single month no matter what the market is doing.

At the same time, they have no incentive to grow our money. As long as the growth rate is 2.5%, they will take their share—even if it means leaving us with zero growth. And if the growth is negative, they still don't lose anything real since all the losses occur on our side of the fence.

In the same interview Mr. Bogle also discusses the dangers of market timing. In his view, only one in a hundred can beat the market. I disagree. I think it's more like one in a thousand. That's because so many people take a casual approach to their investing education. If we get serious about educating ourselves properly, I firmly believe the number of successful individual investors can be much higher.

With a good education on investing, managing your own money seems to me the logical path. If buy and hold is such a good idea, then we would see Wall Street following that approach. But they don't even follow their own advice. Perhaps we shouldn't follow it either.

The Problem Is Always Ignorance

The reason these financial institutions can collect these fees is simply because the public will pay them. They don't know any better. The only reason people hand over their money is because they don't feel they can do a better job on their own. Yet mimicking the market is extremely easy to do as an individual investor. Unfortunately, though, people don't take the time to develop a real financial education. Instead, they get caught up in the culture of searching for a "hot tip" that will bring them riches. They just want to be told what to buy and then forget it.

The problem is not that 401(k) plans fleece the long-term investor. No, the problem is that the investor allows it to happen.

No one forces us to invest in 401(k) plans. It's not like taxes… at least not yet. The educated investor does not need to turn over his money management responsibilities to Wall Street. People can and should do better on their own. And they must do better if they want to salvage the dream of retirement.

Every game has a winner and a loser. Wall Street wants to be the winner, so they stack the deck in their favor. They set the rules so that we are the losers. If you think they are concerned about whether you will have enough money in your retirement account to fly across the country to visit your grandchildren a couple times a year, or do the kind of activities you have been waiting for, or even have enough to pay all your bills, you are sorely mistaken. Their goal is to increase their own bottom line regardless of what happens to yours.

When most people learn about the tyranny of compounding costs and see the truth about how their lifetime of investing is gobbled up in fees paid to the mutual fund management companies, their emotions range from anger to depression. I wish I could tell you that this is the end of the sad story. Remember that $30,000 dollars that was left over in our account after fees? When it's time to withdraw that money, there is still one more unpleasant surprise waiting for you. It's called taxes. And once again, the uneducated will suffer from the ultimate bait and switch.

Chapter Ten

The Great Bait and Switch

It's no secret that the government wants its taxes from us. And with a 401(k), they have built in a way to make sure we give it to them.

What isn't so clear, though, is the way they trick us into giving them even more of our money than we realize in the form of taxes. We are lured into putting money into a 401(k) plan because of the tax breaks we get. The contributions go in before tax, and then our money grows tax deferred until we pull it out. That's the bait.

But what most people don't realize is that the way the government has set up the rules, it is actually a huge tax DISADVANTAGE when we pull that money out. In fact, we're going to see how putting money into a 401(k) account is perhaps the worst possible place to put your retirement investments from a tax perspective.

You Don't Own Your House or Your 401(k)

For many people the two places they have channeled most of their money is in their house and in their retirement plan. But do these things really belong to you or do they belong to the government?

From a certain perspective we never really own our home as long as we must pay property taxes. In a sense, we might say we "rent" our homes from the government. If we don't pay the rent, the government places a lien on your home. So even if you have paid the mortgage on your home in full, property taxes still pick your pocket.

In a certain light the government also owns the money in your 401(k) and allows the financial industry to skim it until they see fit to return ownership to you. While government and the Wall Street elite have been bedfellows for decades, the cartel they have formed today is truly profound. As we discovered in the last two chapters, the financial institutions can make maximum profit on your money when:

a) They take hold of your money, and

b) keep it for as long as possible.

It's not surprising that the laws surrounding the 401(k) are going to try to ensure both of those things. First, get the money with the bait of a tax benefit, and then keep the money with the punishment of a tax penalty for early distribution.

Once they have your cash, it is no longer yours. They won't return ownership until their buddies on Wall Street get a decade or two worth of fees.

If you still think the money in your 401(k) is yours, then try to get it back. The only way to get it back before the allotted time is to buy it back. They own it, not you. They control that money, not you. And the penalty rate you pay to buy your money back is a full 10%. The reality is that you are forced to spend $100 to buy $90. Thus, early distribution becomes unattractive. Your own money seems to become virtually untouchable.

Understanding taxes is not a suggestion but a requirement for the investor. Yet it is largely out of sight and out of mind for the employee. Taxes are an employee's greatest liability by far. Taxes take more money away from the average person than anything else, including our homes.

Consider all of the taxes you pay during the course of a year:

- Income tax
- Social Security tax
- Unemployment tax
- Property tax
- Sales tax

- Estate tax
- Capital gains tax
- Luxury tax
- Gas tax
- Hotel tax
- Food tax
- Beer tax
- Cigarette tax
- Toll bridges
- State registrations
- Various government fees

For many of us, income tax is the largest tax bill we pay. And it's important to understand that, depending on someone's income level, they will be taxed at a different rate.

Ordinary Income

If a person goes to work in the United States and they receive a salary or wage, that income they earn is called "ordinary income." Depending on a person's individual situation they can be required to pay up to 35% of everything they make to the government. This number changes periodically as different groups of politicians get in office. Considering government's addiction to our tax money, it's easy to assume that this percentage rate will continue to climb in the coming years.

Capital Gains

Different from ordinary income, capital gains refers to the profits made by buying and selling something. This can be things such as real estate, gold, silver, stocks, or mutual funds. In the United States, the going tax rate for capital gains is currently 15%.

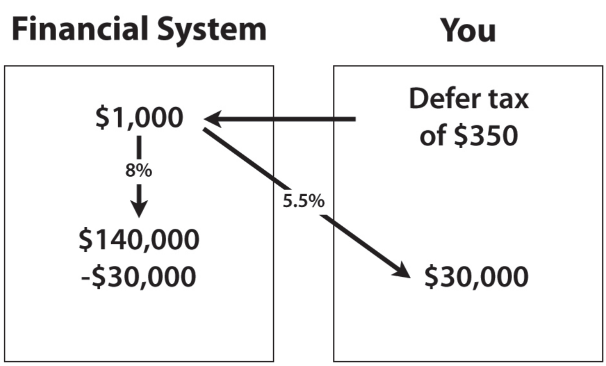
What this means is that a person can pay more than double the amount of tax on money earned as a worker versus money earned as an investor. That's just one of the reasons investors are so keen on investing. The tax burden is much less than that on the money you "work" for.

The Bait and Switch

Looking again at our example in the last chapter, our investor was left with $30,000 in her 401(k) account after giving $110,000 to the financial system managing her money. One of the reasons that an investor would put $1,000 into their 401(k) account in the first place is the allure of a tax deferral.

In the United States tax code there are over 5,000 pages of rules and regulations. Only a handful of pages include instructions on how much tax we need to pay. The bulk of the tax code is a set of instructions on how to defer or reduce taxes through deductions and credits. Our 401(k) contributions are categorized as tax deferred, which means that the tax is paid later when we pull that money out during retirement.

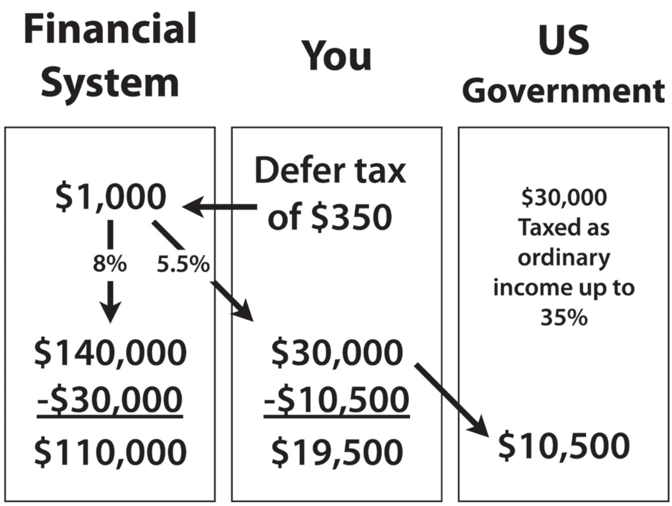
Here is what that tax deferral looks like in our illustrated example:



After we get past the shock of only having $30,000 in our account after all that time it has been invested, it's time to draw it out. On paper, we can show that the initial $1,000 invested was ordinary income because it came from our paycheck and our employer's matching contribution. The remaining $29,000 is profit from market gains.

In a normal investing situation, that $29,000 would be taxed as a capital gain. But this is where the government pulls a sneaky bait and switch on us. For some reason, they don't categorize 401(k) plans the same as other investments. Instead of paying the 15% capital gains tax on the $29,000 increase, the entire account total will be taxed as ordinary income.

Paying ordinary income tax on your 401(k) profits looks like this:



Here's how it works: $30,000 × 35% = $10,500 is paid in taxes. The investor is allowed to keep $19,500 of the account.

However, if it were taxed as a capital gains increase your 401(k) profits would look like this:

($1,000 × 35%) + ($29,000 × 15%) = $4,700 in taxes. The investor in this scenario would keep $25,300 of their account.

So in an effort to defer $350 in tax today, this investor will wind up paying over $5,000 more than needed on the original $1,000 put into that 401(k) account.

Yes, you are understanding this analysis correctly. You can pay up to 20% more in taxes on your 401(k) money than you will on regular investment capital gains.

My good friend Tom Wheelwright is a top tax expert in the world. Tom has a wide variety of professional experience, ranging from Big 4 accounting, where he managed the professional training for thousands of CPAs in the national office, to in-house tax advisor for a Fortune 500 company. Tom later founded ProVision, a company that specializes in helping sophisticated investors reduce their tax liability by proper tax planning and implementing wise tax strategies as well as investor education.

Since I am not an accountant or a tax attorney, I thought it very important to include Tom's perceptive on the tax problem with 401(k)s. I am so grateful to Tom for his willingness to help people discover must-know information about the tax implications of the 401(k) and IRAs that have become so commonplace.

Tom Wheelwright:

"The tax consequences of using a 401(k) are actually much worse than Andy is suggesting. Besides shifting your capital gains from a 15% tax bracket to a higher tax bracket, you are also increasing your overall taxes on your investment income as a result of inflation. Unless you plan on retiring poor, making a lot less money than you did while you were working, inflation will put you into a higher tax bracket when you retire than you would be while you are working. Even without inflation, you will be in a higher tax bracket, simply because you won't have the deductions for your children, your home and your business when you retire.

"Of course, if our only choice were to pay more taxes later or fewer taxes today, we might still decide to postpone our taxes. It's a little like eating dinner. I always like to eat vegetables last because I might die before

I have to eat them. The same would be true for taxes if we didn't have another choice.

"But what if you could permanently reduce your taxes instead of just postponing them? In fact, over 80% of the tax code is dedicated to showing you how to permanently reduce your taxes. My book, *Tax-Free Wealth*, shows entrepreneurs and investors how to permanently reduce their taxes by 10–40% or more. You can find out more at www.taxfreewealthbook.com."

You May Also Be Paying Someone Else's Taxes

Taxation of mutual funds can be as crazy as their fees. Here's another shocking example. Shares of stocks in mutual funds are constantly being bought and sold as people leave the fund, enter the fund, or as the fund manager changes up the holdings of the fund. This means that the fund must pay taxes on some of these transactions.

Guess who they pass those taxes on to? That's right, they pass it on to us as the investors. This is where it gets a little crazy. Depending on when you enter the fund you could actually be paying part of the taxes on these trades even if you have seen a loss since you have been in the fund.

From my research, I think it's about the only time you are required to pay taxes on something you earned no money from.

Plan to Live the Way You Really Desire

I have always been confused with the way many retirement planners set up strategies for their clients. They actually recommend that people plan on living a lifestyle which is less than they are living now because they know the actual returns they will get from 401(k)s and mutual funds are so utterly pathetic. Apparently downgrading is acceptable to these planners as a legitimate way of helping their clients. They literally show clients how to be poorer in the future.

I am shocked that planners don't realize that they are truly sentencing their clients to a retirement of poverty. Not only are these investors being pushed into living on far less income than they are accustomed to, they will also be dealing with higher cost of living prices due to inflation and other economic pressures.

For me, this kind of advice is ill-conceived, wrong, and ultimately harmful.

I believe that given the choice, people will instead want retirement plans that can increase their cash flow throughout their lives and into retirement. To do this may require stepping out of the shadow of the current retirement system because it is not helping you reach your goal. The first step is to begin gaining a financial education about different retirement account possibilities as well as investing strategies and principles to guide your decisions. Learn the language of investing so you can discuss these issues with confidence.

Finally, please don't ever forget that these contribution accounts are designed to be supplemental. They are meant to be a portion of your plan, not the entire plan by themselves. Many people also have additional investment accounts, or real estate holdings, or a business to help them generate cash flow for their goals. Whatever you decide to do, be aware of the tax implications of your decisions. Work with a qualified accountant to help you understand and plan for the tax liability. Proper tax planning can keep you out of trouble and put additional dollars in your pocket.

Chapter Eleven

The Corporate Bankruptcy Loophole

Looking back to the 1800s, I imagine most people in the United States, and probably the world, worked from cradle to grave. A person worked for money or food their whole life unless they learned to become an investor. Building cash flow from one's personal assets was the road to a comfortable retirement. It was most likely a privilege that was earned only by those ambitious enough to learn how to do it and then make it happen for themselves.

But in the late 1800s that all changed with a new idea. A few companies developed a new way to attract and keep good employees with the promise of a free retirement called a pension. Today's idea of retirement is a mere century-old experiment. Like most business ideas, it has gone through the cycle of development, introduction, growth, maturity, and finally decline.

Pension plans offered a chance for the average person to stop working and spend their golden years in leisure. They'd still receive a paycheck, but they'd no longer have to work for it. Retirement as we think of it today was born.

These companies began to attract and retain the best employees by luring them in with this new reward for years of faithful service. The idea caught on like wildfire and soon the American dream changed dramatically. Rather than building businesses or assets for oneself in the spirit of free enterprise, the new dream was to get an education and land a good job with a company offering a pension plan. It revolutionized the university education experience. Degrees became more specialized and focused on a niche rather than a general education. More people wanted to market themselves to work for someone else's established business rather than risk starting one of their own. Retirement has transformed from being an entrepreneurial idea that comes from hard work to an entitlement mindset that people expect as their given right.

Globalization Will End the Experiment of Pensions

It is my opinion that the United States must begin to innovate at a greater pace because many of today's jobs can be shipped to China and India where people will work for just a few dollars a day. This globalization is a job killer for the United States. And it brings to the forefront one of the biggest problems facing U.S. corporations: legacy promises.

A legacy promise is one where the company agrees to pay an employee after they stop working and enter retirement. In 1875, the American Express company pioneered the concept of a defined pension. The invention of the pension was a way to solidify their human capital in terms of recruiting talent and retaining it. Today, pensions are a nightmare for corporations because of their severe impact on the financial statement. Pensions are a massive expense to these corporations that must compete not just with other companies here in the United States, but with companies all around the world.

How does a company burdened with legacy promises continue to compete in this new world? Their competitors are getting talent in other countries for a mere fraction of the costs here, and those competitors are not paying retirees $50,000 a year even though they are no longer producing value for the company.

It's a situation that is becoming increasingly important for companies to deal with. Competitive forces and greed are pushing them to take bold steps to get rid of their pension plans once and for all.

401(k)s Put Pressure on Companies to File Chapter 11 Bankruptcy

Imagine sitting in a corporate board meeting discussing the high costs of pension plans. Everyone in the room is focused on solving the same problem: How to legally burn the contract binding the corporation to fulfilling these legacy promises. The goal is to reboot the company and wipe the pension expense off the books to dramatically improve the financial situation of the company.

In days gone by, corporate bankruptcy was a process to shut down a company when it became insolvent. The process was like administering last rites before the company was dead and buried. At that point, the remaining assets were taken into possession by the courts, sold off, and whatever funds were generated were used to pay off the creditors.

Today, bankruptcy has undergone drastic changes. It is no longer a death ritual; now it is a rebirth ceremony. Look across the corporate landscape and you'll see what I mean. General Motors went bankrupt, and now they are back. Delta Airlines and United Airlines also went bankrupt, and yet they are still flying travelers around the world. Over time, the laws changed so that companies facing true bankruptcy could receive a little protection from their creditors while they renegotiated loans to stay afloat. The original intent for this protection was to help these companies restructure themselves and stay afloat. Helping them stay in business was good for the workers and good for the economy. However, as we've shown time and again, unintended consequences pop up where we least expect them.

Bankruptcy courts and laws are now used by corporations to accomplish their objectives of profits at any cost. To them, restructuring isn't about staying in business for a greater cause. The laws now give corporations the ability to break their promises to employees in favor of more profits. Specifically, they are lining up to break the legacy promises they made to support their employees in retirement with pension plans, health insurance, and other forms of support.

This legal but morally questionable tactic by corporations is proving to be effective in breaking unions. As unions work to gain more benefits for their members, bankruptcy court is making those promises meaningless by legally breaking them under the guise of restructuring. These corporations see it as a way to cut costs. For many it is far less expensive to go through bankruptcy than to keep their pension promises.

If you are a major auto manufacturer, what else do you do when you have sold about the same number of cars as Toyota, but you also have to continue to pay out more to the workers who are long gone from your work force? Bankruptcy has been a blessing in disguise for these amoral corporations. Just file chapter 11, burn all your pension promises, and replace them with 401(K)s. Another win for big business and another loss for the worker.

This is another strategy being used to hunt down and kill defined benefit retirement plans that will lead to their permanent extinction. Remember that it has been just over one hundred years since the first pension plans appeared in the late 1800s. Employers used the pensions to attract the best employees to work at their companies. The idea caught on and became widespread by the mid-1950s. Social Security was added in 1934 as another way to supplement the pension plan. Less than a century later, it appears that both of these systems of retirement income are on their way out.

Traditional Pensions Are Dying

The one-two punch of globalization and 401(k)s have the traditional pension plans on shaky legs. Facing both systemic and non-systemic risk issues, pension plans are quickly becoming insolvent. Some companies made projections that relied on steady stock gains to help pay for those legacy promises. The crash of 2000 caused big problems for companies betting on those big gains. With so many pension plans under pressure and the inability to pay for their legacy promises, it is causing huge problems throughout the entire system. Today the government entity that insures America's corporate pension plans are underfunded by billions of dollars.

When traditional corporate pensions don't have enough money to cover their commitments to former employees, they are taken over by the Pension Benefit Guaranty Corporation (PBGC). The PBGC is a little-known government agency that grew out of ERISA legislation to help protect the beneficiaries of traditional pensions. Congress put the PBGC in place to protect workers from failed pension plans in the private sector. For example, if a union negotiates a pension plan with private industry, the PBGC makes the tax payer the guarantor in the event of a private pension failure. This could lead to this agency paying retirees of failed pension funds up to $55,000 a year, and we foot the bill.

Here is a segment from the PBCG's annual report in 2010:

> *Over the years we've become responsible for almost 1.5 million people in 4,200 failed plans. Every month, on average, we pay $467 million for pensions for 801,000 retirees. PBGC is also responsible for future payments to almost 700,000 who have not yet retired. During FY 2010, we assumed responsibility for 109,000 additional workers and retirees in 172 failed plans.*

All in all, the PBGC covers 44 million workers in over 27,500 plans. Right now the PBCG has a deficit that is an all-time high of $21 billion. Many additional companies are teetering on the edge of poor pension plan ratings, giving the PBCG an additional exposure of $170 billion.

In this environment, companies are either phasing out their traditional pension plans in favor of 401(k) plans funded by employees, or they are taking the more drastic route of entering chapter 11 bankruptcy when the burden of union-supported pensions becomes too much to bear.

The Solution Is Independence

In my opinion, the idea of retirement as an entitlement or a human right is not economically viable for most industries and companies in today's competitive global environment. Financial comfort for the masses carries too hefty a price tag to place on the taxpayer.

The free enterprise system has not forsaken us; we have forsaken it. Free enterprise is an old friend waiting for us to return like prodigal sons. When viewed as an entitlement from a corporation or government, financial independence and a comfortable retirement are fading fast. But for those who pursue this goal individually, it is still not only fully possible, but awaiting your effort. This pot of gold, however, must be earned without the help of government, corporation, or any other institution.

It's on Our Shoulders

Over the course of just a handful of short decades, corporations and the government have teamed with the financial industry to leave the dreams of a comfortable, worry-free retirement in tatters for most people. The institutions we thought we could count on are heading swiftly toward bankruptcy. By all reasonable measures, Social Security and healthcare won't make it. Corporations are abandoning their legacy promises and restructuring through bankruptcy. Financial institutions only use us to generate their own wealth.

Now, it appears the ones who will enjoy a dream retirement will be investors who know how to avoid the pitfalls of 401(k) plans and mutual funds. These are real investors who ignore empty sales pitches and seek high-yield returns and learn to actively manage risk.

Chapter Twelve

Insuring What Matters Most

During the course of this book I have noted several times that there is an inverse relationship between how much control you have over an investment and the degree of risk you take on.

More Control = Less Risk

Less Control = More Risk

No Control = Massive Risk (gambling)

It's important to understand there is no way to completely eliminate risk. We drive to work without thinking much of the possibility of getting into a serious traffic accident, and yet that risk is there. We cross the street at a busy intersection because we believe the cars will stop for us. Yet there is always a chance someone will run the red light. So the issue isn't that we should eliminate all risk, because it's simply not possible.

When it comes to dealing with stock market risk and your investments, there are some basic countermeasures you should consider. Serious investors do not run away from risk, nor do they carelessly jump into risk. Instead, serious investors learn how to manage risk in their favor.

No Insurance for Mutual Funds

Chances are you already apply some of the basic principles used by professional investors in some area of your life. A classic example is fire insurance for your home. We implement preventive measures and practice caution to do the best we can to prevent a fire, but insurance protects us in the event that something unexpected happens. It's foolish to risk all that money you have put into your home without protecting it with insurance, right?

Imagine one of your neighbors complaining that their house burned down and they didn't have any insurance on it. Of course you would feel sad for them, but you would also think them foolish for failing to protect their property. It's a rare thing for a house to burn down in this day and age, but it's not out of the question. Sometimes it just happens. So when the unfortunate does happen and that house burns down without insurance, we're almost tempted to think they had it coming because they let the control slip from their fingers when they chose to not buy insurance.

Earlier we discussed investment goals in terms of our confidence in them actually happening as we predict. I showed you that a goal can be categorized as likely, hopeful, or impossible. We can also turn that around and use those same three categories when we talk about risk.

- *Is it impossible for me to lose my money?*
- *Am I hoping that I don't lose my money?*
- *Or is it likely that I will lose my money?*

We are wise to buy insurance when the riskiness of a situation falls into the likely or possible categories. *Is it likely that my home will catch on fire?* The answer to that question is probably no. *Is it possible that my home will catch on fire?* The answer is yes, it is definitely possible. Therefore, insurance is a very wise financial move in that scenario.

Now let's look at the level of risk we face with a 401(k) account. *Is it possible for me to lose money in my 401(k)?* Of course it is possible to lose money. *Is it likely for me to lose money in a 401(k)?* Considering everything we have seen in this book, from the price of credit default swaps on sovereign debt, to the problems facing fiat currencies, and the coming avalanche of baby boomer stock market sell-offs, there is plenty of data to suggest that the market could be ripe for another big systemic drop. It's not guaranteed to drop, but most honest analysts place it somewhere between possible and likely.

Looking at it from that angle, we are posed with the following questions: If the chance of your home burning down is high enough that it justifies insurance, then why can't we insure our 401(k) accounts? If the amount of money that's placed in the home justifies buying insurance, isn't it equally justifiable to want to insure that 401(k)?

If we compare the likelihood of our home burning down to the likelihood of our 401(k) losing massive value over the next five or ten years, which is most likely to happen?

Now that we know more about what is going on in the economy and within our government, are we more uneasy about the lack of insurance on our home or our 401(k)?

Yes, it would be very wise to insure our mutual funds. Try calling your insurance agent and ask them for a policy on your 401(k). Their answer will be a polite but firm "No." Because when it comes to evaluating risk, no one does it better than insurance companies. They know that your investment in mutual funds or a 401(k) account is a huge risk.

A good lesson to learn is that if something is too risky, no one will be willing to share that risk with you no matter how much money you pay them.

No Loans for Mutual Funds

Real estate is very popular with a lot of investors. One reason is because it doesn't disappear. Even if a real estate investor screws up a deal and loses all of his investment on a deal, the home and the land are still there. The property still has intrinsic value. That's why banks are willing to put their money on the line in the form of a loan, because they know if you default on the loan they will have that property to sell and recoup their money.

As much as we like to think that our credit score is the thing that helps us get the loan, it ultimately comes down to whether the bank thinks the property is worth their investment. You may die, you may no longer have the resources to make the loan payments, or any other number of difficulties—but the property will still be there for the bank.

Business loans are extremely high-risk investments. The exact numbers vary depending on which studies you look at, but it's clear that the majority of businesses fail within the first few years. Yet even in the face of such seemingly high risks the SBA still loans money for people to start new businesses.

However, if you go into your local bank and ask for a loan to buy mutual funds, you'll get the same funny stare you got when you asked about insurance. They just won't do it.

And did you ever consider credit cards? A bank has no problem when we go on a crazy spree to buy furniture, clothing, movie tickets, vacations, fancy jewelry, gold watches, home theater systems, and even groceries with their credit card. Many of the things we buy with credit cards will depreciate to zero in a very short time. How much are those movie tickets worth next week? Will that loaf of bread still have value next month?

If you ask the credit-card company for permission to buy stocks and mutual funds, you'll get the same answer you got from the insurance company and the bank: No way.

- Insurance companies will sell you insurance on pretty much anything you can think of—but they are not soliciting many people to sell them insurance on mutual fund investments.
- Banks will loan you money for real estate, business startups, cars, and other things—but they will not loan you money to buy mutual funds.
- Credit-card companies will let you buy things on credit that will certainly lose 100% of their value in a relatively short period of time—but I hardly believe they would like the idea of buying mutual funds with credit cards.

That should tell us something about the financial industry's confidence in the mutual funds that can be invested in for 401(k) accounts. They are happy to create these investments and sell them to us, but they don't trust them enough to insure them or loan us money to buy them.

The bank will loan you money because they feel confident that the real estate will appreciate over the long term. When you draw a graph of home appreciation over long 20- or 30-year periods of time, the line is in a growth pattern. For the bank, lending money on that type of property is a no-brainer.

However, you can draw a graph showing the trend of the stock market over the same time period and the chart looks very similar to the real estate chart. On the surface, it appears that the stock market is the same kind of smart investment because the value will continue to rise. Why then are banks opposed to lending money to help you build your 401(k), but excited to loan you money to buy a house?

Looking at it from that perspective, it appears that financial institutions—the people who really know what's happening—understand that the broad stock market carries more risk than real estate, more than business, and even more than credit cards.

Even more disturbing is that the general public takes great precautions to insure their homes and businesses against disaster. Yet they don't understand the significant risks with their 401(k) accounts. This lack of understanding means they are generally uninterested in finding ways to insure their precious retirement accounts.

The truth is that 401(k) accounts are totally exposed to systemic risk and they can lose a huge percentage of their value within a few bad weeks of the market, and then struggle for years to get back to even. Personally, I refuse to participate in something with that much uncontrollable risk. When I invest, I demand to have some sort of insurance and a hedge to protect my investments.

Asset Protection

A risk that is often not considered by 401(k) investors is individual liability. We discussed the systemic risk of a market meltdown. But we can lose our money in other unexpected ways besides a market crash.

Very few people that get sued ever plan on finding themselves in that situation. It's one of those things that we never think will happen to us.

Hoping for the best but preparing for the worst is part of smart overall planning in our increasingly litigious society.

Not long ago I acquired a rental property. I plan on holding it and collecting rent for many years. As an investor it is my responsibility to decide if I want to hold that property in my own name or if I want to hold it in a limited liability company (LLC). There is a massive difference between holding an asset personally versus holding an asset in a corporate entity in terms of personal liability and asset protection. It makes sense to want that same protection for *all* our assets including real estate, businesses, and securities.

Serious investors actively use the help of a team. Tax experts like Tom Wheelwright help limit tax liability. Asset protection experts like Garret Sutton help investors protect themselves against other potential hazards such as court judgments. I frequently get to speak with Garret Sutton, a world-renowned attorney who specializes in asset protection and business entity creation. As an advocate of financial education, I highly recommend reading the books Garrett has written on the subject.

At one event I heard Garrett speak on something that many people never think of: *How easily could someone take your 401(k) nest-egg via legal action?*

Imagine how it would feel to reach retirement age only to have a lifetime of hard-earned assets confiscated in the blink of an eye by someone else? To prevent that from happening, it is wise to apply our Probability Analysis here:

- *Is it impossible for me to be sued?*
- *Am I hoping that I don't get sued?*
- *Or is it likely that I will be sued?*

Just as a person believes it is unlikely for their home to burn down, they are foolish not to protect it with insurance. Like the house fire, being dragged into legal action is one thing we hope will never happen. But the possibility is likely enough to demand planning that can protect our hard-earned assets.

Hedge Your Bets

It's true that you cannot buy insurance for your mutual funds the same way you buy homeowner's insurance. But there is another way that stock market investors effectively insure their investments. It's called a "hedge."

The process of insuring your home involves two transactions: (1) the major investment is when you buy your home, and (2) the minor investment is when you buy insurance for the home. An investment hedge is very similar. The major transaction is your primary investment, and the minor transaction is the hedge to protect that investment. In this case, however, the minor hedge investment has tremendous leverage. At the time of the transaction, the hedge cost is relatively small compared to the size of the investment. Just as the value of your homeowner's insurance policy grows instantly when the fire begins to burn your home to the ground, the value of the hedge grows exponentially if your major investment begins to tank. That small initial cost for the hedge produces protection that is equal or greater than the value of your major investment.

This basic illustration shows you how professional investors are able to sleep soundly at night knowing they are protected no matter what the market does. If it takes off like a racehorse, their major investment gives them massive profits and their hedge was a small price to pay for that peace of mind. And should the market go down in flames, they'll thank their lucky stars they were smart enough to buy the hedge to protect their major investment.

In essence, the hedge helps to offset the downside potential of your primary investment.

The Irony of the Options Market

Part of the campaign to convince us that we're not smart enough to manage our own investments is what we're told about the options market. We're taught to steer clear of options because they are too risky.

While options can provide tremendous leverage, they can also get you into trouble if you don't know what you're doing. But so can borrowing a lot of money to buy an office building or opening a scuba shop. The key is to use education to reduce your risk. And that's exactly what many smart investors do with options—they use this market to reduce their risk by providing a hedge against large stock market investments.

So why don't the 401(k) companies tell us about this? Perhaps they're so busy telling us the virtues of diversification that they don't have time to mention the value of hedging the broad market with leveraged Exchange Traded Funds (ETFs) or options. It's not like they don't know what those things mean. Even worse, I sometimes wonder if they might be intentionally hiding this concept so they don't risk losing our accounts when we find there are other ways to invest our money.

In addition, these powerful hedging strategies that can be learned by anyone do not easily fit into their assembly line approach to investing. Their giant cookie cutters don't work on individualized plans. Therefore, they don't help us protect our investments using these proven tools and strategies. Instead, they continue focusing on their marketing machine and feeding us more lies to fill their coffers.

Yes, hedging takes time, effort, and skill. But so does shopping for the best insurance for your car and your home, and getting the best rate on a bank loan. If we are truly interested in growing and protecting our precious retirement investments, it's worth every moment. Personally, I like the fact that there truly is a way for me to protect my investment positions with insurance through hedges.

The Stock Market Entrepreneur

Previously we talked about the way the mutual fund industry has brainwashed us into thinking about investing:

Be patient... stay the course... don't panic... you're in this for the long haul.

Those words conjure up an image of a wise old man like Benjamin Franklin endorsing this time-honored tradition of investing. One can imagine people just like us investing this way for centuries.

On the other hand, how does our culture represent stock market traders? They are typically shown as greedy, high-risk gamblers who will do anything for a quick buck.

In my opinion, both of these pictures are false. The first one is meant to lull us into false comfort, and the second to shame us into believing that's what we will become if we do it ourselves.

I like to think about investing the same way I think about business. Some people work as employees, and some people build their own businesses as entrepreneurs. The "employee" type of investor is the one who invests in cookie-cutter investments such as 401(k)s. With no thinking involved, they can just do their thing and enjoy life. Later, when they look back, they often have regrets and wish they would have taken charge of the situation to generate greater returns and satisfaction.

The "entrepreneur" investor, on the other hand, looks at the investment possibilities before him and sees endless opportunity. He may not know how to do it all right now, but he has the confidence to figure it out. Why? Because he sees other average people who have succeeded at it, and he is at least as smart as they are. So he focuses on improving his education and then seeing if his new training works in the real world. Sometimes he wins, sometimes he loses. But at every step he is learning from his mistakes and discovering ways to avoid making them again. As time goes on, his confidence builds and his profits grow. Just like the entrepreneur who starts a new business and builds it over a period of time, the stock market entrepreneur grows his own money-making effort.

At the end of the day, it's true that money cannot buy happiness. But in our quest to give ourselves the kind of retirement that we deserve after a lifetime of hard work, money can be the difference between truly enjoying all of the wonderful things that life has to offer and continuing to work just to survive.

With a 401(k) system designed to funnel wealth to the big financial institutions and laws that have the unintended consequences of sentencing many to lifelong work to make ends meet, what can a person do to break free of these constraints?

The answer is the same as with nearly every problem we face in life: self education and effort.

Chapter Thirteen

How to Take Control of Your Future

When I was a boy my father made a constant effort to teach me to avoid the attitude of being "problem centered" and have an attitude of being "solution centered." We had sort of an unofficial rule that if you were going to complain about something or point out a problem you also had to bring possible solutions to the table and offer ideas on how to correct the very thing you were complaining about. With that in mind I wish to shift the focus of this book in the concluding chapters away from the problems of the 401(k) system to a focus on how one can begin to solve the problem of retirement independently—without dependence on a 401(K) plan.

The problems presented by the current 401(k) system are so broad and also so deep that it is difficult to summon adjectives and superlatives that are too extreme in describing them. In writing this book I felt it extremely important to help people sufficiently understand the breadth and depth of the challenges, risks, and problems brought to us by the 401(k) system for one solitary reason: that the readers could begin to make independent preparations to help mitigate the risks involved, and take proactive action steps to be sure that their retirement dreams do not remain merely as dreams, but have a likelihood of becoming a reality.

Possible as Opposed to Easy

One of the things that makes 401(k)s a flawed concept in my view is that they are presented as easy. We're led to believe that all they require is participation rather than expertise. Remember this?

Work and buy mutual funds

Work and buy mutual funds

Work and buy mutual funds

And of course someday you are supposed to be rich…

It seems to me that some people have lost the stomach for doing things that present a challenge, doing things that stretch oneself, doing things that place us directly on Robert Frost's *The Road Not Taken*. The problems inherent in 401(k)s are formidable and daunting, and so it makes sense that many of the solutions would require far more than just a casual effort towards building one's dream of retirement. Earlier I mentioned that just because someone owns some investments, that doesn't necessarily mean that they are an investor, any more than owning a scalpel makes one a doctor, or owning a briefcase makes one a lawyer. People are what they are based on their education, experience, and proficiency in certain areas, not because of the items in which they have invested.

So in shifting this book from a focus that identifies problems to focus on possible solutions, it's essential to quash the myth that there might be some effortless fix, or worse yet, some piece of legislation that will instantly right the ship. The solution begins by bringing into focus some salient truths that we know have been proven to yield success time after time. The devil is truly in the details, so we must prepare for dealing with the finer points of an investing plan by building a foundation on solid principles.

Re-enthrone the value of working hard and smart.

Success comes with a commitment to work very, very hard toward our dreams. That commitment is not described by a mere willingness but rather by a consuming desire. A steady commitment to work hard in the sowing process with an eye of faith in reaping what we sow. My wife grew up on a dairy farm and she demonstrates that strong work ethic that we have come to associate with relentless chores that offer no weekends or holidays. If I can be so bold, it's my opinion that that type of work ethic is an endangered species in much of the world today.

Some say that working smart is an alternative to working hard. "Would you rather work hard or smart?" they ask. I say if it's not hard then it's not really work. Working smart just brings a better harvest. It brings a higher yield.

So that is truly the first question I think a person needs to begin with when considering the goals they have for retirement. Are you willing to work hard as an investor?

Sadly, many people are willing to work eight to ten hours a day to earn money but are unwilling to dedicate 30 minutes a day to investing it. "I don't have time to fool with investing" they say. It's not a priority. They mistakenly think they can get a harvest without sowing their own seeds. They just want to be a farm hand and get paid to grow the dreams of others. But they don't want to plant and care for their own seeds.

People who are unwilling to work at investing are all about getting tips and boilerplate financial advice so they can keep investing at arms length. Moreover many people are satisfied with plans that plan for mere survival as opposed to abundance. However, in a time where more and more countries around the world have embraced the idea of freedom and free enterprise, striving for anything less than abundance is a very sad waste of opportunity. Considering the price that is paid for the gift of individual freedom, such a satisfaction with mediocrity might be an insult to those who gave the gift.

I have a business associate who lives by the mantra "Dream big or don't dream at all." He came to the United States in his college years from Malaysia. He's a tremendous example of fulfilling what in the United States is called the "American dream." That simply means that we maximize the opportunities afforded to us by the freedom that has been paid for with the blood and the lives of so many.

I'm constantly going to seminars and workshops to try and improve my financial education. Inevitably I also wind up in a "motivational seminar" from time to time. I think these motivational meetings are healthy to a point, but certainly being motivated is no substitute for getting the work done. Meetings, however, are different than classes. Meetings help us feel motivated but classes help us learn. There are a lot of people caught in the book and tape syndrome. They feel that if they can listen to recordings in their car or read enough books on becoming wealthy, somehow it will happen by osmosis. They feel their context will change and they will magically receive wealth.

In these books on performance, individual growth, developing effective habits, tapping the secrets of the universe, thinking about growing rich, or becoming the leader in your field, there's a lot of talk about success. For example one of my favorite programs was developed by the tremendous personal development expert, Earl Nightingale. I'm a huge fan. In one of his excellent programs he defines success as "the progressive realization of a worthy goal or ideal." That's a great definition of success and I adopted it for many years until I heard the following expression while sitting in church one day. I think this nails it on the head. I think it's a perfect definition of success:

"To fulfill the measure of your creation and have joy therein"

Success is to become what you were designed to become. An apple seed must become an apple tree and produce many multiples of itself to be successful. That's what an apple seed was designed to do. Anything less than that, the apple seed did not fulfill the measure of its creation.

Often during the holiday season, like many parents, I dread the words "some assembly required." When I see these words I know that I'm supposed to assemble something: *Wheels, tires, handlebars, pedals…*plus the instructions to put it together as a bicycle. Unless it becomes a bicycle it is not successful because it has not fulfilled the purpose for which it was created. Without assembly the bicycle does not become what it was supposed to become. I think people are a lot like that. It's a great question to ponder as you consider what type of investor you are supposed to become or at least have the potential to be. Anything less than fulfilling our potential is falling tragically short of becoming what we are really capable of becoming. Even if a basketball player wins the game by way of a mediocre effort, he or she is probably not a successful player, because they did not become what they could have become.

I think this is a large part of the solution to the problem of retirement. Perhaps as a person invests a small amount of time in a quiet place where one can contemplate, they can have moments of clarity and truly understand the opportunities that are theirs. We have unparalleled potential to become investors in our day and age. In a 1999 speech, former SEC chairman Arthur Levitt stated:

> *"With so much at stake, all of us must do our part to realize the promise of our markets, and more importantly, the promise of our lives. All of you have the power and means to be the most informed generation of investors in the history of our capital markets. The ease of today's technology isn't an excuse to do less. It's an opportunity and a mandate to do more; to learn more; to be aware of more; to be informed of more and to achieve more—as individuals and as a country."*

The potential we have in the world today makes becoming an investor more doable than ever before. What's amazing is Mr. Leavitt made that statement over 10 years ago and in the 10 years since, his statement certainly applies more today than when he spoke those words in 1999. The truth of the matter is we do live in a unique time with extremely difficult problems to overcome, but we've never had as powerful tools, training, and information resources to allow us to be successful as we have today.

Entrepreneurial Spirit

As I travel the world I'm always impressed with the patriotism people feel for their own country. I love traveling abroad because most of the time I feel humbled as a guest in another country and very grateful for the hospitality of the citizens. They always seem to have a very deep desire to introduce me to, and encourage me to experience, the very best of their foods, traditions, and culture. I feel the same way about my own country, the United States. I think one of the mistakes we make when we teach our children about America's founding fathers is that there might be so much emphasis on things like the Declaration of Independence, the Constitution, and the Bill of Rights at the expense of focusing on the people that immigrated from all over the world to participate in that great experiment of free enterprise.

I've alluded to this earlier in the book, and I think it's worth revisiting now in greater detail. There was much more to the success of the United States in becoming a world power in such a short time than merely the establishment of the Constitution. Consider the requirements to become a citizen of the United States in the early history of the nation. Saying that it was formidable is an understatement. America had become known as the land of opportunity. They were risking everything for the opportunity. Just to have a chance. Just to have a shot. For many people at that point in history, there wasn't even an opportunity to dream in their own country. Property rights were for monarchs not peasants.

Think of what it must've taken just to arrive in that land of opportunity. It meant that most would have to say goodbye to their family and friends forever. It meant leaving behind everything you had that wouldn't fit in the small trunk to make the journey by ship. Many people embarked on a ship across the Atlantic without knowing the language they would need to learn when they arrived.

Upon arrival to this land of opportunity there were no substantial guarantees of any kind—other than the opportunity itself—but simply the chance to pursue happiness. It was a place where anyone had property rights and the opportunity to build something and call it their own. There were no healthcare programs. There were no Social Security programs. There were no unemployment programs.

I think it was a tremendously high risk yet high reward environment. Many people were losers. Many people went hungry. Many people died of illness. People came to the United States knowing that they were literally risking their lives. All the Constitution did was provide an environment for people to have an opportunity to succeed. An opportunity to become the best they could be. It was not the Constitution that made the people successful. It was the people who made the Constitution successful. That would be a great lesson for legislators of the world today.

Those first-generation Americans had to pass tests that had everything to do with life and death. I imagine it takes a certain type of person with a certain type of backbone, desire, work ethic, and passion to be able to take such tremendous risks just for the chance to succeed with no guarantees.

At first glance, it would make sense that every rising generation would have a head start over the generation before them. They could stand on their shoulders without having to risk life and limb for opportunity. At first glance one would imagine the likelihood of success with each generation would become greater and greater. But on the other hand, each generation has been given the same opportunity but without offering the large sacrifices. Their backbones would not have to be as strong. Requirement to participate would be reduced each generation. Perhaps we are learning today that the opportunity also needs the backbone to make it work. Today's typical U.S. citizen is not an immigrant. Today's typical U.S. citizen grows up speaking the language. Today's typical U.S. citizen was born in a country where they were very unlikely to die of starvation.

So it's quite possible that because the opportunities afforded in most free enterprise systems were not purchased by the sacrifice of those in the system today, there is a lack of appreciation for what it means to dream big. There is not the same context of work, sacrifice, and most of all the risk of losing big. America is no longer a high-risk/high-yield environment. I hope I'm not being unpatriotic when I say that the entrepreneurial spirit is something that is embraced by the minority rather than the majority.

If there were to be a new "early-America-like" opportunity in the world, I wonder how many of today's Americans would make similar sacrifices as most immigrants. I wonder if they would sell all they had to come. I wonder if they would say goodbye to their friends and family forever. I wonder if they would emigrate to a land that had no healthcare system and no social security system, but allowed you to keep much more of what you create.

The Entrepreneurial Spirit Makes Retirement a Project Rather Than an Event

I think to take full advantage of the opportunities of any free enterprise system it's important to have an entrepreneurial spirit. It's important to tie retirement dreams to a project that is worked towards daily with specific tasks that bring the end result. I think this is the context of an investor. I don't know how it is for others, but I know it's the way I feel. When we begin to ponder life's possibilities and life's opportunities and our own potential, entrepreneurs feel moments of deep desire to set to work and create something special for their family.

I feel inspired to learn more, to experience more, and to rely less on the systems at large, particularly corporations, governments, and institutions. The 401(k) plans seem to have a certain appeal to those without an entrepreneurial spirit because they deal with minimums, or adequacies for survival. In conversations related to 401(k)s, words like "sufficient" are used much more frequently than words like "abundant." The entrepreneur/investor is much different. Their aim is to leave a legacy. To become the best they can possibly become. Being adequate is not enough. They want to fulfill the measure of their creation. They want to become who they believe they were designed to become.

If at this point in this book you are less confident about the 401(k) system to provide you with the retirement you've always dreamed of… that's probably a good thing. If at this point in this book you feel motivated to take some actions and take matters into your own hands, that, too, can bode well for your future. If at this point in this book you feel a sense of urgency… then I believe that the first move you can make to place yourself on the path of reclaiming your retirement dreams is to begin to fan the flames of your entrepreneurial spirit.

In the next chapter I will introduce some more specific actions or basic investing strategies that are available to almost anyone. But before anyone decides to pursue becoming a true investor, I think it's wise to take some personal time and think about your own entrepreneurial spirit. Chances are there's a powerful resonance you will feel when you ponder ideas like self-sufficiency, independence, achievement, being the best you can be, offering value to others, and making the most of opportunity. When you feel that resonance, your goals will become larger. Your desire will run deeper. Your passion will grow greater…your resolve, more stubborn… your satisfaction more serene.

When it comes to retirement, most people talk about it by using the word "have" or "having." They think of all the things they want to have. Please know that the true journey to retirement is about the word "becoming" not "having." The entrepreneur thinks about what he or she wants to become, and then they set to work to become what they feel they were designed, even destined, to become. They settle for nothing less.

Do you want to become a skilled investor?

Chapter Fourteen

Respect Your Financial Education

Almost any free enterprise system offers everyone the invitation to become an investor.

Some choose to be workers for money and decline the invitation to become skilled investors. Much of our education system begins with the end in mind that the student will acquire some skill, or some kind of knowledge that will allow them to work for money. Yet all of us know, or at least should know, that to align ourselves with the true principles of wealth building we should not work for money, but rather we should learn to skillfully have money work for us. That's what skilled investing is about. To have money work for you, and that is the opposite of what our current education system teaches or instills in the majority of students.

Problems Can Be Identified Quickly

Though the problems with the 401(k) system that we've chronicled are vast and desperate, the gravity of the situation can be surmised in the reading of a simple book like this one.

The good news is we can identify the problems readily and within a few moments that can act as a spur to help us correct things. We don't need to study year in and year out to come to an adequate understanding of these problems. Understanding the problems is more of an intellectual exercise and not a developmental exercise. Problems do not need to make the entire journey down The Education Continuum™.

If we can graduate from ignorance to awareness in the context of identifying a problem, that is entirely sufficient. Once we get to that point we can then place our energies into becoming true investors.

The Solution Will Take Effort Because it Requires Development, Not Just Awareness.

Remember that one of the flaws in the 401(k) system is that it promises something that it does not deliver, namely: results without effort. That's why Chapter Two of this book is called The Ignorance Myth.

Because the problem is identified quickly people might mistakenly expect a solution to simply come the same way, that is to say, merely to be identified. That would be a popular idea to sell because, like the 401(k) program, it requires no effort, just mere participation in what is sold to be sufficient.

Part of my commitment to the reader in this book was to tell the truth whether it was popular or not, or whether it was comfortable or not. The truth is that becoming a skilled investor is much more satisfying that just shaving off a portion of your paycheck to buy mutual finds on autopilot. They that pursue this journey have an indomitable entrepreneurial spirit. The entrepreneur gets excited about the work of investing. The 30 minutes they spend each day investing their money becomes much more satisfying than the 8 to 10 hours a day they slave away earning it.

Entrepreneurs get energized diving into projects that require challenge and positive energy. They get excited about climbing a mountain. They get excited about trying to accomplish things that are hard. There's even a part of them enjoys managing the risk of failure—and then winning!

It's Simple: No Shortcuts

One of the large industries in the world is the weight-loss industry. Like the 401(k) program, it's filled with hyped promises of success that eclipse the disclaimers.

Losing a few pounds is a reality for anyone who wants to go to work and follow rules. I have a friend that makes it very, very simple when it comes to any discussion on weight loss:

Eat less and move more.

Everything else is just fluff. A person has to show discipline in their nutrition choices and discipline in their exercise routine. End of story. People try to market potions, lotions, pills, equipment, regimens, routines, dietary supplements, and contraptions of every kind. But it's no replacement for hard work and discipline. The challenge of such a realistic and down to earth message is that non-investors are always looking for something instant and free. In their search for a quick fix they often forget the reliability of work. The fact is we can all lose a few pounds if we eat less and move more. And once a person simply embraces that fact, they can have what they want.

I believe the same is true with investing. There's no "new" investment will magically solve one's problems.

Investor Education

It's very clear in reading this book that the challenge is not the legislation that allows for 401(k)s, or the institutions that propagate 401(k)s, but rather the ignorance of the individual investor that becomes a victim of the other two.

If taking a personal inventory and strengthening a person's entrepreneurial spirit is the first step, pursuing a first-class investor education is the next. Financial education will become the next chapter in education evolution. The way we view education as a society has not always been the same. Like anything else, our view of education adapts and changes based on changes in the environment.

My great, great, great grandfather was a German immigrant to the United States. In Germany he was a respected academic and would regularly visit with his colleagues in the libraries of Germany and discuss philosophy. These men would light their pipes and discuss how the universe worked in the world of science. They would speak about arts and literature and all the other branches of education.

In 1857 he came to America and, after a time, became the teacher in his community. Though he is now remembered and revered as one of the great academics of his time, he was not always thought of with such reverence.

In the early days he was not very well liked by some. Many of the people in the community viewed him as shiftless and lazy because he was a teacher. Many people in those days valued a good hand on a farm much more than a man who sat in the schoolroom teaching children about mathematics and literature. He was occasionally looked down upon because he didn't have the calloused hands the farmers did.

In our private family history there are stories where after school he would literally call on the parents of his students to see if he could get a chicken or perhaps a few tomatoes for compensation as the neighborhood teacher. Many would ridicule him and ask, "Why don't you go out and do some hard work for a living?" In parts of his community there was extreme contempt for education.

Gaining an education seemed to be a second-class idea because most people would wind up working on the farm anyway.

Understanding Shakespeare, Plato or Socrates or things like mathematics seemed to have little value. In his lifetime there was a massive change in how we view education, as the Industrial Revolution was about to come into play. Later on in his life he became the first president of what stands today as one of the largest private universities in the world. Today people see the value of education and see that the difference between a first-world country and a third-world country is simply education.

As the world has continued to evolve, so has education. It has been a story of the need to acquire more and more to stay on top. In the old days, going to high school or going to work on the farm were both acceptable choices. Soon, however, it became very important to have at least a high school education.

At one point going into college or perhaps going into the military or even going into the work force were all acceptable alternatives. Now we teach our children to strive for a college education in the hope of landing a good job and higher income. To discourage a child from getting a college education would be frowned upon in today's paradigm… a far cry from where it was in the days of my great granddad.

Yet when it comes to financial education I sometimes feel much like my great grandfather might have, because of the tremendous lack of respect for financial education today. For the longest time financial education has been an idea that's far ahead of its time.

From time to time I'm invited to teach financial workshops. Generally these workshops have a tuition associated with them. They are not motivational in nature, but instructional. Many uneducated people scoff at the idea of education that improves upon their college degree. Yet many others are realizing that it's okay to invest our time, our money, and our energy into learning new things after high school and college. Particularly when it's education on topics that were not covered in the curriculum of high school and college.

My great, great grandfather was made fun of and scoffed at because he felt that what he was teaching the children had tremendous value—perhaps even unlimited value to both individuals and to his community as a whole. Yet many people thought that investing in such silly ideas as learning math and literature were a complete waste of time and frivolous investments to the point where some might even have thought them fraudulent.

As our world evolves today it's more and more clear that college education is no longer sufficient. The vast majority of people who attend my workshops are college-educated. They're in attendance because they're lacking and they have the meekness to understand that. If their college education alone were sufficient to help them reach their dreams for retirement, they wouldn't feel the spur to learn more.

Now that the 401(k) system has all but destroyed the defined benefit pension programs, a college education that helps people learn how to become an employee is simply increasing the likelihood that a person can be a lifetime employee. College now helps people increase the likelihood that they can work until they die. Why? Because now there are very few pension programs where companies will pay you until you die. In the past, being an employee could get you 30 years of work and then another 30 years in retirement. Now becoming an employee only gets you 30, 40, 50, or even 60 years of work.

The evolution of education has always been a requirement to receive more and more. When grammar school was no longer sufficient, high school became a necessity. When high school was no longer sufficient, college became a necessity. Now that college is no longer sufficient, supplemental financial education has become necessary if a person wants to become an investor in today's world.

Trial and Error

I suppose it's possible to receive one's financial education in the school of hard knocks. However the tuition in the school of hard knocks can be pricey. Some have lost hundreds of thousands of 401(k) dollars in the school of hard knocks. However, the biggest issue in terms of retirement is that people are running out of time. Trial and error is very time intensive. It takes time for people to figure things out on their own by making mistakes. Therefore the evolution of education isn't simply about adding more class time on different topics, but also the very approach to how we learn.

Evolution of the Learning Experience

One of the biggest weaknesses of traditional education is that most things are taught in the abstract. The ratio of class time to field trip is lopsided. Often we can go along The Education Continuum™ in the abstract to the point of competency.

As investors, competency is not enough. One must complete the entire journey to proficiency. It's a lot like the swimming lessons that I purchased for my son. Swimming lessons are ineffective when taught in the classroom or read from a book.

Imagine if I were trying to teach my son to swim by having him study the chapters in a book or perhaps listen to some recording while we ride in the car. He would be no more ready to swim than he was at the ignorant stage. Some learning must be experiential. It's done little by little in increments, but it's done in the environment that you anticipate gaining proficiency in. Of course my son's swimming lessons were conducted in a swimming pool. Much like the metaphor we gave in the example of nutrition and exercise, of the lesson of eating less and moving more, there are no shortcuts in learning how to swim. There is no infomercial we can watch and call a 1-800 number to purchase a product that will give us the ability to swim.

Becoming a skilled investor is the same thing. It requires experiential learning in addition to the theoretical learning that occurs in the classroom. This is why authors can sell millions and millions of copies of books on the topic of wealth and investing, and yet the readers are able to invest no more effectively than my son could swim by reading a book.

Some people study theology at length in hope of discovering the purpose of life. Many of those who do come to the conclusion that man's life on earth is educational. To learn certain things like good and evil. If that's true the good Lord must have seen fit to teach based on experience. Certainly we wouldn't have to hassle with this life if we were merely to make an intellectual assent alone. It seems sufficient that God could've set up the classroom or given us a book to read without us having to hassle with this earthly experience. But theology aside, there's no question that there's no substitute for experience, and the brain learns best by immersion and active experience. Consider the teaching methods that are used traditionally in school as opposed to what could be the most effective in terms of education.

Less Effective	More Effective
Books	Experience
Tapes	Labs
Lecture	Mentors

Learn with Constant Mentorship

Perhaps one of the greatest moves a person could make in becoming a skilled investor is to find good mentors. A person can harvest the costly mistakes of others without having to pass through personally and invest so much tuition in the school of hard knocks. Warren Buffett had Benjamin Graham. Donald Trump had his father. Many other entrepreneurs jumped past college and delved right into experiential financial education. They sought the help of mentors as opposed to staying at Harvard or Yale. There's often just simply not enough time to fulfill the education requirements mandated in school when specialized education is what will really help us begin with the end in mind.

Mentors are very different than teachers. They often give feedback that is more immediate and severe. I think a great example of this was my college basketball career. I was not a very good basketball player, but I had some wonderful coaches and mentors. My chemistry professor was very much indifferent to my performance on my chemistry tests. She felt that her job was simply to throw out the information.

My basketball coach, on the other hand, was extremely hands-on. Poor performance was not just penalized with a poor grade but rather very intense and immediate penalties like running stairs or doing push-ups until my arms could no longer move. The reason for such powerful feedback was because there was a time constraint. The game was played on Thursday and we had very little time to prepare.

We had to move from ignorance all the way through proficiency to have success in a short period of time. Hands-on daily mentorship and practice by experience was necessary. It couldn't be done on the chalkboard alone. We had to practice executing our offense and defense on the floor so we'd know how to do it again in the game when the pressure was on.

Many people know that I serve as the paper assets advisor in the Rich Dad organization, led by Robert and Kim Kiyosaki. The mission of that organization is to increase the financial well-being of mankind through financial education. Robert Kiyosaki is probably best known as the author of the greatest personal finance book of all time—*Rich Dad Poor Dad*. What I think is lost on many people is that it is actually a story of mentorship. Remove the 'Rich Dad' from that equation and everything changes.

Books Are Not as Effective as Classes

There's a reason that people have to go to class in college. Books can only take one so long and so far. I'd be far from confident in the abilities of a cardiac surgeon if all he completed was a home study course and had read a few books on the topic. There's no replacement for live instruction on a particular topic. So as you begin to pursue your education, my counsel to you is to have respect for your financial education. Know that you will get out of it pretty much what you're willing to put into it. Never short cut the process or short change yourself.

Financial Education is Finally Gaining Respect

I often think of my grandfather trying to get a chicken or tomato in exchange for the valuable lessons he was teaching the children of his community. Hopefully today we are much more advanced than the farmhands that would ridicule him. "Real value is hard work on a farm," they would say. Imagine someone today not understanding that a knowledge of mathematics is far more valuable to their child than a chicken or tomato. It turns out that it was the farmhands that were ignorant. In their pointing fingers at my grandfather and accusing him of laziness or even fraud, they displayed their own ignorance and stupidity.

In this day and age, financial education is finally emerging from the cloud of misconception as the "get rich quick program." In the past many of the alternative education resources such as workshops, seminars and webinars, have been ridiculed as having little value; "real value is a college education and nothing more." Adding to or taking away from a college education is a sin in the eyes of some folks. They think formal education, especially at the college level, is complete.

Yet today alternative education is proven for many to be a life changer. More and more of the private sector is starting to understand the value of financial education. Within the last five years one of the largest stock brokerages in the world—one that specializes in online trading—acquired a small brokerage for the sum of hundreds of millions in cash and stock. What many people don't know is that one of the major components of that small online brokerage was its investor education program. This education program had and still has levels of tuition associated with it to the tune of $20,000 and higher. While it doesn't even remotely approach the hundreds of thousands of dollars demanded for traditional college degrees, it demonstrates a legitimate investment that shows a true commitment to financial education on the part of the investor.

Certainly this online brokerage saw the value associated with the investor education program. After acquiring this new business, additional resources were placed into their educational programs.

Yet before this acquisition and other events that have legitimized financial education, there were many who treated those that offered it like my grandfather: "Why in the world should someone have to spend money to learn how to trade stocks?"

We can't discount that those with no financial education tend to lose multiples of the tuition investment in poor decision-making and in their misunderstanding of risk. Many 401(k) programs in this country have lost hundreds of thousands of dollars or more. Financial education is justified in our day and age in terms of time, energy, and money.

The Basic Investments

As you consider your own entrepreneurial spirit you'd be wise to consider which of the different types of investments or combination of investments are most suited to you and what you want to achieve.

Businesses

I was visiting with a friend of mine who's been an entrepreneur his entire life. He spent a very short time in college where he played baseball for a while, and then decided to leave school to strike out into the business world. He has had successes and setbacks, and most recently tremendous success again. Recently I was visiting with him and was explaining why I was writing this book.

As intelligent as he is, I may as well have been speaking to him in Japanese because his context is so far from that of an average employee.

His mindset is simply about building a bigger business with increasing cash flow every single quarter. He doesn't worry about retirement in terms of minimums or what would just be sufficient to retire. The idea of not working anymore has never entered his mind because he's in control of his own business and can take time off anytime he wants. He loves his business and has passion about the mission of his business. He loves offering value to his customers.

Unlike the employee who can't wait to stop working, he can't picture himself having more fun doing anything else. He already enjoys the trips to Hawaii and plenty of time away with family. He enjoys driving fine automobiles and living in a beautiful home. He also enjoys the entrepreneurial thrills of achievement and the personal growth that comes with taking things to a new level.

Many people never consider starting a business as a means to retirement. Why not? Maybe it's because it's never been presented to people when they were in school. School seems to be about getting a job. Becoming an entrepreneur to build for the future is a high risk game to be sure. But it's also high reward. It certainly gives an opportunity to thrive… where an employee's 401(k) is usually about survival.

Make a list of things that you enjoy. Make a list of people you know. Make a list of talents that you have. If you were to list six activities you enjoy, six successful people that you know and respect, and six talents that you have, it's likely that there's a million dollar business idea somewhere on that list.

I have a business that I very much enjoy because I get to do it with my friends. Sometimes our more casual business meetings occur over a game of HORSE on the basketball court. We enjoy the flexibility owning a business allows us. Certainly there are times where the stress levels achieve new highs and the learning curve becomes very severe, but that's when the entrepreneurial spirit kicks in.

It's not my aim for this book to strike fear in the hearts of people regarding 401(k)s. What would be most satisfying to me is to see many of the readers become inspired and determined to start their own business and take on the retirement problem head-on in an innovative, independent way.

Real Estate

I've had several real estate mentors in my life. While I would not yet consider myself a real estate expert I've enjoyed income from having investments from real estate.

What got me interested in real estate was a comment of one of my real estate mentors made long ago.

Just One More House

He suggested that I ponder some of the people I know who are older, that might be struggling financially in their retirement years. He asked a very simple question: What if they would've simply bought just one more house? They were able to buy one for themselves to live in. Surely people could learn to buy just one more. Then over the next 30 years allow the renters to make the payment until the home is paid in full at retirement. While it might not be a matter of multimillions in assets, how much would their life change if they had bought just one more house?

Pondering the question had a profound effect on me and made me realize that the sooner a person begins to learn about investing in real estate the better. What would even an extra $1,000 a month mean to someone who is dependent on Social Security alone?

What if a person became determined to become a skilled real estate investor by gaining the proper education and learning the tricks of the trade in the hands of an experienced mentor? Any time, energy, and money spent attending real estate seminars or courses would pay huge dividends. It's education that is truly life-changing in retirement years.

For me, becoming a doctor or lawyer was not in the cards because there's no way I have the intelligence to compete in classes like organic chemistry and physics with all those smart guys. But I wonder how difficult it would be to teach someone to acquire 8 or 10 homes over their lifetime. It seems to me like it might be the better venture for some when compared with the rigors of medical school or law school. At the same time there would still be hard work with no free lunch. A person would have to become an investor just like the doctor had to become a doctor and the lawyer had to become a lawyer.

Is Real Estate Investing Riskier than a 401(k)?

Real estate is one of the basic needs of life: food, clothing, and shelter. People will always need a place to live. It seems to me that God is always making more people and the population of the world grows each year. But it doesn't seem that God is making real estate at the same pace. Those two ideas alone make learning how to become a real estate investor as legitimate an idea as praying for the stock market to rise. In Chapter Three we learned about systemic risk and attaching our dreams and goals to the mood swings of the stock market. Having something concrete like a little real estate couldn't hurt—especially if the investor had an education on how it's done right. If that person learns how to properly use debt, they can effectively insulate themselves against much of the ups and downs of the real estate market.

So if you feel that business is not your game, perhaps real estate can be. Becoming a real estate investor is not on the same par as trying to become a Bill Gates or Steve Jobs in business. The rules of real estate could be studied and learned just like any occupation such as accounting, plumbing, or being a zoo keeper. It's a realistic venture for the single mom, or the student right out of high school. It can be an alternative for the father who was just laid off from his job. It can also be done part-time, so it is suitable for the accountant or the engineer who sees their 401(k) statement pushing the retirement finish line farther and farther into the future.

Stocks and Options

Of all the possible investments we can make, stocks and options are dangerous simply because they're so easy to get involved in with no education. Someone who's ignorant in business is going to fail long before he's even able to raise enough capital to get the business running. Someone who is ignorant in real estate must at least get to the point of securing financing to make any big mistakes. But the lowest financial IQs on the planet can buy stocks or mutual funds. So while investing in stocks and options should not be viewed as any more or less risky than starting a business or investing in real estate, its 'ease of entry' often makes it quite perilous.

In some ways, starting a business is like trying to fire a gun that's locked away in Fort Knox. It takes a lot of know-how and smarts to even get into Fort Knox to get your hands on the gun.

Real estate investing would be like a gun locked in a gun safe. You'd have to at least figure out the combination to the safe before being able to fire the gun.

Investing in stocks and options is like having a gun in your hand with a bullet in the chamber and the safety off. It takes almost nothing to be put in a position to fire the gun.

Some people say that investing in stocks requires the least amount of financial education. That's true if you're talking about mere involvement. But if you are talking about doing it successfully, it requires just as much financial education as the other investments we have discussed.

The irony of the 401(k), is that it ignores many of the advantages that stocks and options bring such as:

- Liquidity… the ability to buy and sell readily
- Agility… the ability to make money in up markets and down markets
- Leverage without debt

The options market is mistakenly stereotyped as a high risk instrument when the truth is that many options are purchased to limit risk, rather than for speculation.

Learning to write covered calls in the market for income is an absolutely legitimate strategy. It can be done in a Roth IRA with significant tax benefits. In fact the stock market is extremely versatile to the educated investor.

The Truth Hurts, but it Makes You Free

In the Introduction to this book I promised you that the message in these pages would be harsh and blunt. That's because there is no other way to tell this story. Very few are spreading this word, and the problem is getting worse.

I have tried to describe for you a realistic scenario of what lies ahead for 401(k) plans and the investors who trust them. Even though various government acts may have been created with honest intentions, we have seen how the Law of Unintended Consequences always seems to creep in and deliver something very different than what was originally planned. Unfortunately, it's not the lawmakers who pay for these consequences. That burden falls on us.

As I discovered for myself how the 401(k) plan was doing its part to dismantle the American dream, I knew I had to do something about it. One of the goals of this book is to strip away the salesmanship and shiny paint that the massive financial institutions are using to cover up the truth about these plans. We are a culture influenced by good marketing. When given the facts, however, it is our responsibility to protect ourselves and act in our own best interest.

If you have read all the chapters of this book, you might be feeling angry, scared, or depressed. Perhaps even a combination of all three. If so, that is a good reaction. You should have some kind of negative emotional reaction because you are now aware of the lies you have been told about your retirement accounts. As you have peeked behind the curtain, now you know for yourself why the numbers are not adding up in your favor.

But please don't let that be the end of it. No matter what your current financial situation is in regard to your approaching retirement, you should never give up. Like any sports coach will tell you, the game is never over until the final whistle blows. Even in the face of all the bad news you have read about in this book, your own game is not over yet.

New People Are Creating New Wealth

If you think your retirement situation is bleak, open your eyes and look around. In our society there are those who enjoy wealth and those who struggle to put food on the table every day. It's not fair, is it? But that's the reality of life.

As you look at those who struggle and those with wealth, one significant difference is financial education. Those who have gained a solid education about how to get money and grow it into wealth tend to establish their position on one side of the fence. Those without that education typically find life to be very difficult.

Here's the good news: With every generation, there are always new groups of people who discover that it's absolutely within their reach to gain wealth for themselves. Creativity and knowledge are their keys to the treasury.

Yes, it's easy for most people to watch TV from the sofa and ignore their retirement investments. That is exactly what most people will do. But now you have the knowledge that a hands-off approach simply will not get you where you want to be.

Over my years of teaching people how to take charge of their investments, I have seen people from all walks of life transform themselves. When they decide to accept the responsibility for their financial success, they realize it doesn't matter how much money they have at that moment. Their first big step is to have faith in themselves. By taking this leap of faith, they are allowing themselves to open their minds and learn new things. They are giving themselves permission to turn away from the sputtering 401(k) system and step boldly into a bright new future filled with knowledge and opportunity.

I issue the same challenge to you: Have faith in yourself! Realize that you have the ability and intelligence to manage your own investments with more wisdom and passion than a 401(k) management company could ever provide. Create a dream for your future and then gain the skills and knowledge to make it happen. Others have done it before you, others are doing it right now, and even more will make their dreams come true in the future. If you decide to take that step, do it with full confidence.

Look Before You Leap

I participated in one particular event that was different than any other. The meeting had no agenda, and had no speakers. Instead, I served on a panel with some very prominent experts from various financial fields.

There were about 300 people in attendance who were free to approach a microphone and ask any question to the panel. A young lady asked me a question that I think many people will after reading this book: "Andy, I know you have been somewhat critical of 401(k) plans. Can you tell me how to get my money out as soon as possible?"

I answered her question with one of my own: "If I were to show you how to do that, what would you do with the money?"

"I would invest it," she said.

I responded, "What are you going to invest your money in?"

"I don't know," she said.

I suggested to her that perhaps she had misdiagnosed her problem... that perhaps she felt her problem was the 401(k). When in reality for her and most people the problem has nothing to do with 401(k)s, or IRAs, or mutual funds, or any other retirement plan.

Her problem was simple. And it's the same problem that most 401(k) participants have. They don't know HOW to invest.

REMEMBER: 401(k)s are not the real problem. The problem is not knowing how to invest.

Before you decide it's time to move your money out of your 401(k) right this minute, first take a deep breath. It's not wise to jump from the frying pan into the fire without a plan. Remember, the first leap of faith I referred to above is to have faith in your ability to learn and grow.

If you are determined to manage your own investments, you first need to educate yourself. You need to know how the markets work. You need to identify your own goals. You need to gain the knowledge and confidence required to make smart decisions.

There are many resources available for individuals to improve their financial education. I try to keep my students informed about the best training resources I can find. If you would like me to keep you informed feel free to join us on this journey of financial education at *www.andytanner.com*.

My goal is to make financial education simpler, easier to understand, and truly life changing.

This is your moment to stand up and shine. Now is the time you choose to boldly step out from the false shelter of the 401(k) system and create your own future.

As always, I'll be here to help you in any way I can.
Andy

About the Author

Andy Tanner is a renowned paper assets expert and successful business owner and investor known for his ability to teach key techniques for stock options investing. He serves as a coach to Rich Dad's Stock Success System trainers and as the Rich Dad Advisor for Paper Assets.

As a highly sought after educator, Andy has taught tens of thousands of investors and entrepreneurs around the world. He often speaks to students at the request of Robert Kiyosaki, showing how paper assets can fit into the Rich Dad system of investing. In 2008, Andy was key in helping develop and launch *Rich Dad's Stock Success System*, which teaches investors advanced technical trading techniques to profit from bull and bear markets.

He is the author of two books: 401(k)aos and the soon-to-be-published *Stock Market Cash Flow*, a Rich Dad Advisor series book on paper asset investing.

Andy has also created an online investing course called *The 4 Pillars of Investing*. You can find out more about it at www.4pillarsofinvesting.com.

Other Books by
Andy Tanner

Stock Market Cash Flow
Four Pillars of Investing for Thriving in Today's Markets