Testimony: Ric Edelman
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I am honored to present testimony today before the Subcommittee on Social Security and Family Policy of the Senate Committee on Finance.

In short, the ASPIRE Act is a brilliant idea, and I highly commend Senators Rick Santorum and Jon Corzine for sponsoring this legislation. I can say that this idea is brilliant because I had the same idea – and brilliant minds think alike. I also get to brag that I thought of it first, although yours is an improvement in several important ways. Let me explain.

I am a financial advisor and founder of Edelman Financial Services, the largest independent financial planning firm in the nation, based on number of clients, according to *Bloomberg Wealth Manag*er. My firm manages more than $2.6 billion in client assets for more than 7,000 individuals and families. Unlike the vast majority of advisors, my firm does not work primarily with the high-net worth market. Instead, we cater to middle class families who want to achieve financial and retirement security.

I also host radio and television programs on personal finance, and I have written 5 books, including 3 national best-sellers which collectively have sold more than 1 million copies. I also host a financial education web site, www.ricedelman.com, publish a monthly newsletter and am very active in financial literacy activities.

Several years ago, I invented the RIC-E Trust® - the Retirement InCome – for Everyone Trust®. This is a retirement planning tool for children that is so unique it has two U.S. patents (6,064,986 and 6,085,174). So far, approximately 2,800 RIC-E (pronounced RICKY) Trusts® have been created.

The idea was inspired several years ago by a caller to my radio show. He said his wife had just delivered a baby and he wanted to save for this new son's future. When I began explaining how best to save for college, he interrupted me. "I'm not talking about college," he said. "I want to know how to save for his *retirement*."

I was stunned – and told him so. "Nobody saves for a baby's retirement!" I exclaimed. The entire notion is preposterous – we all know how hard it is to save for *college* – can you imagine the cost of saving for a baby's *retirement!?!?*

To prove my point to him – while still on the air – I pulled my financial calculator from my briefcase and quickly punched in a formula. If you set aside $5,000 at birth and leave the money untouched until the baby is 18 and ready for college, assuming a 10% annual return (the average annual return of the S&P 500 Stock Index since 1926 is 10.4%, according to Ibbotson Associates), you'll accumulate about $27,000. That's not enough to pay for college today, let alone 18 years from now.

But that same $5,000, at the same 10% return, if left invested for 65 years, would grow to $2.4 million!

Contrast that with the experience of a hardworking American who dutifully saves in a 401(k) plan for an entire career. Even if a worker saves 10% of pay every year from age 20 to age 65, and even if that worker chooses the right investments the entire time, that account will be worth – if the worker is lucky – only about $750,000. By comparison, a one-time contribution of just $5,000 produces more than three times as much!

The reason, of course, is the magic of compound interest. Never before has anyone tried to grow money for such a long period of time. Yet, that's the key to retirement security.

Unfortunately, there are two problems with my simple math, and I explained them to my caller. First, my calculation did not adjust for taxes. If you have to pay taxes annually on the account's profits, you won't end up with $2.4 million. Instead, assuming a 33% tax rate, you'll accumulate only less than $350,000 – rending the value of the effort hardly worthwhile. Second, if you set aside money for a child, the child at age 18 gets legal access to that money – so the real question is not wondering what the account balance will be at age 65 but, rather, what color the sports car will be when the child graduates high school. Indeed, based on my nearly 20 years of experience counseling thousands of families, I can assure you that if the child can spend the money, he or she will.

Even if the child refrains from a frivolous splurge, it is still unlikely that the account will survive intact all the way to retirement. Why? Because we all encounter financial issues during our adult lives – the need for a down payment to buy a house, large unexpected medical bills, sudden job loss, marital or family problems and more. Being able to tap into an account often is too tempting to resist. Only later, in retirement, do people express regret.

So, the harsh realities of taxes and access burst the bubble of the idea. But I was convinced there was a solution, and that finding a solution could translate into a huge benefit, not only for America's babies, but for the next generation and, by extension, all of American society.

It took me two years to overcome the tax and legal hurdles these problems presented, but I succeeded and as a result the RIC-E Trust® was introduced in 1998. Although designed for newborns, a RIC-E Trust® can be created for anyone of any age (although, obviously, the younger the beneficiary and the later the benefits are received, the more the account can grow). The trust is irrevocable, meaning that money contributed cannot be accessed until the beneficiary (the child) reaches retirement age (which is set by the grantor upon creation of the trust; it cannot later be changed and cannot be less than age 59½). There are exceptions for the child's disability (he or his parent/guardian gets the money) or death (his estate gets the money for distribution to heirs). This solves the access problem.

To solve the tax problem, the trust invests the money in a variable annuity, which allows the money to grow tax-deferred until withdrawal. This allows for tax-free compounding over decades, just like an IRA. The money can be invested in a wide range of asset classes – stocks, bonds, government securities, real estate funds and more.

There is a one-time set-up fee of $300 to establish a RIC-E Trust®, and there are the typical fees charged by annuities. There are no other expenses – no annual fees, no custodian or trustee fees, and no annual income tax, nor any tax reporting or preparation. The minimum investment is $5,000 and additional contributions can be made at any time in amounts of $500 or more. But other than voluntarily adding money to the account, the RIC-E Trust®, once established, is completely hands-off. Time will do the rest, with quarterly statements issued to the child and grantor.

The program envisioned by the ASPIRE Act is much better than my RIC-E Trust® for two reasons: first, it is automatic for every child in America; mine requires decisive action by parents and grandparents, and of course requires them to have financial ability to contribute $5,000 for each of their family's children and grandchildren. This puts the RIC-E Trust® beyond the reach of the vast majority of Americans. Second, if the ASPIRE Act operates similarly to the federal Thrift Savings Plan, the operating expenses would be extremely low – much lower than those of private-sector variable annuities like the one my RIC-E Trust® uses. These lower costs can translate to higher account values for the children.

I have only two concerns with the ASPIRE proposal. First, I would prefer that the account be restricted to retirement. Currently, it also can be used for education and buying a home. This is not necessary: with the advent of student loans and mortgages, both college and home ownership have become pay-as-you-go expenses. Nobody pays cash for a home anymore. Instead, they pay for it while they live in it – if they move, they sell the home and use the proceeds to pay off the mortgage. Similarly, nobody needs to pay for college up-front anymore. Instead, students can get through school via loans, and then repay those loans over the course of their 40-year careers. This is not only an acceptable approach, it is increasingly the only approach that is viable for today's college students.

But you cannot pay for retirement on a pay-as-you-go basis; it is the one major expense that *must* be paid for in advance. After all, you can't save for retirement while you're in retirement, and for that reason, I recommend that the ASPIRE Act restrict distributions to retirement age, with exceptions for death and disability. Otherwise, we face the risk that many will spend the proceeds long before they reach retirement age.

Second, since the proposal already permits Americans to make additional voluntary contributions, I would recommend that these limits be increased. While the program should not become a tax shelter for the rich, raising the ceiling to the RIC-E Trust®'s level of $5,000 would be of value to middle class and upper middle class families, and would result in larger numbers of Americans being able to reach retirement age with a higher degree of retirement security. This, in turn, would reduce their dependency on government in their elder years, freeing the government to focus its resources on other important needs.

I fully realize that the establishment of accounts under the ASPIRE Act would put my RIC-E Trust® out of business, rendering it both redundant and more expensive than the ASPIRE Act's federally sponsored version. This would cause me economic harm.

Go ahead and do it. It's the right thing to do for Americans, and for America. And I will do everything I can to support this initiative and help it become law.

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