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Are you playing rational roulette with your retirement plans?

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We all know that our mental abilities will wane at some point, though we like to think it won't be until extreme old age. Is it possible that those abilities diminish sooner and faster than we think, even in the absence of dementia? If we look around us, we can find objective benchmarks that suggest this is indeed the case.

Take chess, which seems like a purely mental pursuit, as an example. Surely players keep on improving with experience and practice. Yet, among the top 30 players in the world, no one is older than 47 and only six are over 40. On the other hand, 16 of the top 30 players are under age 30 and the No. 1 and 2 ranked players are just 25 and 23.

When a specific intellectual capability can be measured objectively, it can be shown to decline with age. It is obvious with highly esoteric pursuits like chess, but more insidious with the more mundane intellectual activities, such as managing our investments or choosing appropriate insurance coverage.

One study of older Americans attempted to measure financial acumen at different ages. The subjects, who were aged 60 to 88, were given a test that required basic knowledge, memory and problem-solving skills. This test proved to be quite a challenge. The average score for 60-year-olds was about 60 per cent correct, which is barely a pass. Test scores actually rose a little up to age 65 but after that, they fell rather steadily. By age 73, the average score was less than 50 per cent and subjects in their 80s did not even reach 40 per cent.

While this might not come as a great surprise, what was most intriguing was that the older test subjects were more confident of their abilities than their younger counterparts, even though they scored considerably worse! It is this age-related hubris that we should find most troubling.

While this is a sensitive issue, it needs to be addressed since the combination of declining mental skills and rising confidence levels suggests that pre-emptive measures are in order. I recommend that everyone should make the most important decisions regarding their financial affairs no later than in the first stage of retirement. At that time, they should also put into place an action plan of how and when others will be brought in to assist (or take over) the decision-making process in the later stages of retirement.

For instance, you should have a clear idea of how conservatively you want to invest your retirement assets and how the asset mix might change over time. This can be decided and written down when you are 65 so you don't have to worry about it at 80. A partial list of the areas where financial decisions can be made early on is given in the accompanying table.

You will not necessarily delegate these decisions to your grown-up children when you reach a certain age. For one thing, they may not have the skill-set to make the decisions themselves and, for another, they may be conflicted because your interests and theirs will not always align. Think about an annuity purchase, for example: There have been instances where the grown-up children of an elderly retiree have tried to block the purchase of an annuity because it cuts into their inheritance.

You might be thinking, why take action now? If you find yourself failing and think you need help, you can ask for it then. Such a reaction is not unusual. As financial planner Rona Birenbaum puts it, most of her older clients want to “hold onto every expression of their independence for as long as they possibly can.” By doing so, however, they are engaging in a form of Russian roulette — or what I call “rational roulette.”

The problem is, you will not really know for sure when the time comes to hand over the reins to others. You might currently be 30 or 50 or even 70 years old and know with absolute certainty that you’ve still “got it.” The trouble is, when you start losing it, you will still think you’ve got it. How do you differentiate between your current state of being absolutely certain of your cognitive abilities and a possible future state when those abilities are waning but you don’t realize it? Some things are better not left up to chance.

Illustration by Chloe Cushman/National Post

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Fred Vettese is Chief Actuary of Morneau Shepell. This instalment is one of the themes explored in his new book, “The Essential Retirement Guide: A Contrarian’s Perspective” which is being published by Wiley for release on Dec. 14.

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