Assessing the Value of a Financial Advisor and Developing a Comprehensive Financial Plan

This paper will discuss the critical importance of developing a financial plan for retirement.
What do you miss by avoiding the process?

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If you are uncertain that you need a financial plan for retirement - you are not alone. Many families or individuals have contemplated whether they need a financial advisor or financial plan.

Is there actual value and benefit to you?

Before I answer that question, I completely understand where you are coming from and let me give you a little background as to why.

For the past few decades, Wall Street has continuously put its own interest in front of ours – the hard-working middle-class. Whether it is high-fee products, sales commissions or lack of transparency, these are all examples of how Wall Street decided their interest was more important than yours. I know this because I spent two years working for an investment bank.

This created an emphasis on having a stronger sales culture versus a culture of advising and acting in the client's best interest. Consequently, over time, the financial services industry fell further and further down the list of most trusted professions. (Gallup, 2016)

Looking back, it makes complete sense to me. For many decades, you experienced high-pressure salespeople trying to sell you products you did not necessarily need.

The metaphor of a doctor writing a prescription without diagnosis or testing comes to mind. A reputable physician would never do this! Ironically, doctors and nurses rank near the top of the most-trusted profession.

Why?

For starters, they create a comfortable process and experience for you to understand and improve your health. When you walk in to medical clinic you will typically fill out a form requesting information and background; then a nurse will take you to a room to check your vitals and ask some more detailed questions regarding your medical history, what is bothering you and previous experiences.

Eventually, the doctor comes in for further analysis, discussion and questioning. All of this handled *before* any prescription or solution has been written.

Unfortunately, far too many financial sales people were running around selling prescriptions before diagnosis. In my opinion, committing financial malpractice!

The good news is that slowly this is changing. Regulations are making it more difficult for the product sellers. Consumers like you are getting smarter and realizing they need advice, not another product. Technology is also creating more transparency, which benefits the consumer.

All of this is great for you - the future retiree.

This paper will help you discover and understand what to look for in a financial advisor and the value you add. Most importantly, a logical process to creating a financial plan will be unveiled.

What do I look for?

Not to sound too cliché, but it all really comes down to building trust. Unfortunately, trust is not earned over night - it takes time.

In a minute, I will explain why building trust is one major advantage of going through a financial planning process. Before that, I have included some framework to help you interview a perspective advisor.

Below are questions I would encourage you to ask a financial advisor/planner before you go down a path or enter an agreement with them:

1. Have them tell you about their background, family and career path. *(You learn a lot about someone by hearing his or her story and where they have been.)*
2. Do they create financial plans for their clients?
3. How are they compensated or paid?
4. Do they act as a fiduciary for their clients? Do they have any conflicts of interest?
5. What is their investment philosophy?
6. How do they communicate with clients and the frequency of interaction?
7. What are the biggest risks they see retirees facing? *(What is important to you is not the same for everyone else.)*
8. What makes them different from the next advisor? (*Hopefully great service is not there only difference as that should be the standard!)*

You will learn a lot about them by asking these questions and begin to feel either comfortable or resistant to moving forward.

What is the value?

In September 2016, Vanguard published research titled: *"Putting a value on your value: Quantifying Vanguard Advisor's Alpha."* In their research, they concluded that the value of proper financial advice could add up to **3%** in potential net returns.

The criteria was broken down as follows:

- Suitable asset allocation and diversification
- Cost-effective investments
- Rebalancing investments
- Behavioral coaching
- Asset location
- Tax-efficient withdrawal strategy

This is very powerful, telling research from one of the largest investment managers in the world. Clearly, there is substantial evidence to back up this report.

Additionally, Morningstar created their own report published August 28, 2013. *"Alpha, Beta and Now…Gamma"*

Their research concluded that a qualified financial advisor could add an additional **1.59%** of net return and estimated an additional **22.63% increase** in retirement income could be added. This value was created through asset allocation, annuity allocation, dynamic withdrawal strategy and asset location.

Type	Additional Income Generated	Gamma Equivalent Alpha
Total Wealth Asset Allocation	6.43%	0.45%
Annuity Allocation	1.44%	0.10%
Dynamic Withdrawal Strategy	9.88%	0.70%
Liability Relative Optimization	1.65%	0.12%
Asset Location/Withdrawal Sourcing	3.23%	0.23%
Total	**22.63%**	**1.59%**

Both of these research papers highlight similarities except Vanguard put further emphasis on behavioral coaching. Regardless, these are both very trusted sources within our profession and these findings should not be taken lightly.

My experience would agree that there is unmeasurable value in behavior coaching, but more importantly trust. Clients who trust their advisor should feel more at ease if we are doing our job properly – then allowing the client to focus on their family and the things they enjoy.

Developing a Financial Plan

There are many different ways to create a plan – some good and some bad. My experience has allowed me to create hundreds of plans for families and analyze what has worked well and what has fell short. If you avoid planning and enter retirement without understanding the dynamics, you are likely missing valuable information about your future.

Obviously, I know most of you are not going to enter retirement without a plan.

Current perception is that a financial plan needs to be a big, thick document with all kinds of charts and graphs. All this does is cause confusion. For some, a financial plan can be very simple with 3-5 core assumptions or actions that need to be followed. It is different for everyone.

Through my experience in dealing with baby boomers, I have created a process that addresses many of their concerns as well as educating them on what are the various risks they need to be prepared for in retirement.

If you have read my latest book, *"Stress-test Your Retirement: Creating a Plan for an Every-changing Economy"* you will discover how I feel it is important to compare and test many different potential outcomes for your retirement and how they relate to one another.

Below are four valuable stress-tests that we run for all of our clients.

1. **Retiring earlier, Living longer**. According to EBRI, more people are retiring before the age of 65 than they anticipated. Additionally, life expectancy for both male and female continue to increase due to medical advancements and technology. **Do you understand the impact of early retirement and longevity to your retirement? Do you have the assets and income to weather this storm and not run out?**

2. **Taxes.** With 10,000 baby boomers retiring each day, our budget expenditure for Medicare, Medicaid and Social Security are likely to increase. With more expenses, means more tax revenue needed. This will likely lead to higher taxes at some point.

   Many retires are already surprised how much they are still paying in taxes. Ways to minimize taxes and create flexible, tax-efficient distribution is another important stress-test. For many, much of their retirement savings has been accumulated in tax-deferred accounts (401k, IRA). Guaranteed income is typically from pensions and social security.

   All of these sources are subject to Federal income tax. **Testing strategies like Roth Conversions, the order of distribution and distributing based on tax brackets are valuable exercises to tax-mitigation.**

3. **Investments.** Far too often static rates of return are assumed to determine if a person will have enough assets for retirement. Unfortunately, that is not realistic. Average rates of return need to be coupled with some level of volatility or fluctuating sequence. Testing what rate of return is needed to avoid running out of money is critical, but that should be taken one-step further. The sequence of returns and risk tolerance need to be added. **What is the least amount of risk my family can take is a great scenario for testing.**

4. **Optimize Distribution.** Each of us has different resources for income in retirement – pensions, Social Security, working part-time or retirement savings. These resources are different for each family. Unfortunately, there is no one-size-fits-all formula optimizes retirement income.

   Example: Although it is advantageous to wait to take Social Security, it may not be the best solution once you factor in your future income gap or needs. Understanding how different income sources work together to maximize income while minimizing risk and taxes is a critical exercise.

Conclusion

The Compound Effect is a principle belief that a series of small incremental changes over time reap large, exponential gain.

This principle cannot be truer when it comes to retirement planning.

I challenge you to ask yourself, "Do I have all the resources needed to do the absolute best for my family's future?"