Sound Financial Bites 056 - Paul Adams

Episode Transcription

> *"What we wanted to do with our 'design and build' model is we sought to create a safe learning environment."*

Hello, Paul Adams here. Welcome to Sound Financial Bites, where we help you with bite-sized pieces of financial and life knowledge to help you design and build a good life.

Hello, and welcome to Sound Financial Bites. My name is Paul Adams. I'm your host for today's episode, as well as the President and CEO of Sound Financial Group. I got to tell you, I'm so glad that you tuned in to today's podcast. We're going to talk about some things that most people don't talk about when it comes to financial advisors, when you're trying to get advice, when you're trying to get help, and that is the way the advisors make money.

Now, what we're doing here at Sound Financial Group is we're actually in the midst right now -- well, we've completed this shift of changing our compensation methodology, the way that people choose to engage us and the way that we work with them over time in a way that we think is going to make a much bigger difference for every single client when they work with us, allow them to take the work that we do together more seriously, and allow them to feel like they can really get the help without the little voice in the back of their head wondering whose interests are being held when they're working with us.

So, that's kind of the topic of today's podcast. But, before we get to that, I also want to mention one thing. Over the next few episodes, we're going to continue here at Sound Financial Bites, and what we're going to also be doing is building a new podcast. There's going to be more coming on this, but what I want you to know is it's really going to meant to be targeting people that are our clients: those people that make between 300 thousand and a 1.5 million a year, those people that are effectively what you would call in the top 1%, those people whose household incomes are north of about $350 thousand a year.

And once a month, that new podcast is going to interview somebody who's broken through to that top 1% income, and we're going to call it View From the Top 1%, and what will it take for you, if you're not yet there, to be able to get there. Now, this is not going to be some kind of podcast that has people thinking that anybody is looking down from the top 1%, but rather, once we've broken through that top 1% from an income perspective, what is it that we are doing to better steward that level of income that's coming in.

What are we doing both in the way of charitable giving, what are we doing in the way of managing our finances. Because, let's face it, most of the financial advice that's out there for everybody today has got to target 90% of the population. Why does it have to target 90%? Because, the new shows need 90% of viewers to tune in so they can sell advertising. The magazines need 90% of people to buy the books, and they need to buy the magazines, publishers need them to buy the books. What we see is that all of the advice that comes out there is not tailored for the folks that we work with, or the folks that we work with who they're trying to grow into.

So, we want to be able to not only bring them financial content that's appropriate, much like we've done here, but a more focused effort in helping people to get to that higher level of income, and those that get to that higher of level of income, help them be better stewards of their time so that they can design and build a good life the way they want it, not let the almighty

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"Clients can layout the aims that they want to have and know that they've got somebody in their corner."

dollar rule them.

In fact, what might happen is some people may listen to the podcast and take away that they're perfectly happy making a quarter of a million dollars a year. That's a good income. Instead, what they're going to do is instead of playing the game of getting more income, what they're going to do is play the game of, "How can I spend more time with my family? How can I spend more time in my recreation or in service to my community?"

So, I'm really looking forward to that. You're going to watch that coming up the next several weeks. We've got to build a lot of stuff to release it, but I'm excited to give everybody on this podcast a sneak peek of what is coming.

So, let's get to the way advisors are compensated. What I think most people accept as common and no big deal is that the way most advisors are compensated is on commission-based products, or frankly, even a fee-based advisor that's taking a 1% fee every single year, or sometimes 1.5% a year, is that none of them are getting compensated unless you transact with them.

So, what that's developed, and even a model of that in the past I was certainly swept in, was that what we had to do is sit down with a client, and show them some ideas, and get them to take action on some products. Now, that never sat well with me. I didn't like the idea. I didn't like how it felt selling stuff to clients.

So, what I did many years ago - this is going back almost 15 years ago - is I built a value-added process to help clients look at their entire financial life, both those things that we would help people with, and things outside of what we did to help them make better decisions on everything from their car insurance to their real estate by giving them a wide-angle view that they could see their money in.

What that did for us, as an organization, is it made it so I didn't have to "sell products". What I was able to do is educate and coach my clients for the last decade and a half all on the basis that what I hoped is I would bring enough value that they would transact, and that was certainly what we experienced. Somewhere in the area of 95% of people, if they got to the point, after the first couple of meetings with us, that they chose to engage, we found that they would end up transacting in some way about 95% of the time.

Now, that worked well. Though, the problem is, in the background, in the back of everybody's head, I could watch it. I could hear it when we're working with somebody by GoToMeeting where sometimes there was a shift, and that shift would be, "I wonder whose interests he really has at heart," and that caused us, because I didn't like that feeling, to get really rigorous on how we would show people our strategies, doing our best to show indisputable math and independent scholarship for any recommendation. As a result of using indisputable math and independent scholarship, we could kind of break through what could be a concern for the client around a perceived bias or an interest.

But, this is how it's been working for financial advisors for over 100 years. In fact, if you're listening to this right now and you're working with an advisor, nearly guaranteed, when you engage that advisor, you're in the position that the advisor had some meetings with you, looked at some strategy da-da-da, and then at some point, there was a transaction and you had to buy some insurances, or you had to roll your money over to them, or acquire an annuity, or if you're a business owner, take over your 401(k) or take care of some things there.

That's been the way it is, and everybody's sort of accepted that that's the way it is. Except, other industries solved this concern many, many years ago. Let's just look at architecture. If you wanted to have plans for a building that you were building for a long time - we're going to talk about how long ago architecture's been around - you would engage somebody to do the drawings, and you would engage somebody to design what you're going to build, and then separately, you would engage for the building

"Nearly everything in life will draw us away from taking the time to build a future to meet the aims we're after."

Now, we've talked for years about this idea of design and build a good life, but what we're adding is this idea that what we need to do is have a design build process. This design build process will put our clients in the position where they know they're engaging for the design, where they can work with somebody and that person is going to actually help them decide what that future should look like and what kind of financial components they should bring in to take care of that future. Then, separately, we're going to have the offer to build it if they want to.

So, what I want you to think about is a design build architecture firm where the architect does the design, and then perhaps that firm also owns a general contractor that could build it. Think about this. We don't go -- and we have got great clients that are general contractors, and general contractors are used to consult their specialized knowledge, and yet we don't go to the general contractor directly to do the design, because that's a separate stage of the process.

So, what we're doing with the design build process is we're actually making two offers to every client where they can engage us for the design only. Separate engagement, separate fee-based agreement for the design. Then, if they want to, they can have us build it.

Now, for those of you that are existing clients, right now, this could be hitting you a little bit, because the title of this podcast is "Why fees and why now?" So, it could get your attention like, "Oh my gosh, here's Paul." We are grandfathering our existing clients under this agreement so that you can be in a position to know that we are not breaking our commitment to you in what we've done in helping you in the past.

What we are going to do is we're going to engage all of our new clients a little bit differently, and there's more on that in this podcast, but also some things I hope you could take away about how you might reflect on your own business or how would you even kind of step back from the financial current in the way that everybody thinks about money right and be able to make better decisions for ourselves and for our families in the way that we engage for planning of all stripes.

So, let's talk about architecture. Now, there are some really, really old written works that talk about architecture, and they go all the way back to first century. In some of these writings, what they did is they broke apart three different components that are important to architecture. One is durability: that's a building should stand up robustly and remain in good condition. Utility: it should be sustainable for the purchase of which it is used. And beauty: it should be aesthetically pleasing.

Now, if we engage an architect to build that building, they engage for a fee, and they give us the design. As a client of an architect, we have the ability to take those designs and take them anywhere we would want to have them built. Or, if it's a design build architecture firm, we could also have it built with them. Now, you see, what's important is that the client owns what the architect built.

Now, of course, if it's a design build architecture firm, not purely architecture, they have a deep-vested interest in making sure that the client had a good experience, because they'd also like to be that master builder or general contractor to help the client implement the vision that they sketched out in their designs. But, the client can still go anywhere they want.

But, let's talk about the current model for financial advice. We know that what happens is the advisors end up building plans that seem to inevitably involve products that the advisor can put in place in the client's life and be compensated on. You see, a client, oftentimes, will ask questions. We see clients all the time asking questions like, "Should I buy a rental property? What's the best mortgage that I should get? What's the most efficient and effective way to pay for college? How much money should I leave in my business? How am I going to exit the business one day? Then, what's the best way to use the capital in my retirement plan?"

Now, what was interesting as I was talking to a client just a couple of days ago and they had money set aside in 529 plans. Now, not surprisingly, I asked, "Why did you do a 529 plan?" They said, "Well, our advisor said that was going to be the most effective way to pay for college. So, not surprisingly, the answer for the most efficient way to pay for college was a financial product.

Now, that may or may not have been the most efficient financial product to use, but when I even suggested that that might not be the most efficient way to pay for college, and if you read our book, Sound Financial Advice, one of the things you quickly discover is there's some real viable alternatives to funding college that don't involve setting money aside into a 529 plan.

But, it hit because there was another financial person in the room when I was doing this, a CPA, and when I hit the chord of, "This may not be the most efficient," I began to get these questions that were like slightly above oppositional in the way that they were kind of sniping the questions out, and I don't mind having other advisors in the room. I've always believed that if you're not cheating, you don't care who's watching you take the test, and yet you can see how quickly it was in affront to that traditional way of being that we wouldn't just put it in a 529 plan to solve it.

So, customarily, the advisor comes with a list of products to solve the woes for the client. But, the problem with that model is that when the advisors only compensate it by products or only compensate it by doing assets management, which by the way, make no mistake, that's still a product. That advisor that only does asset managing, if he just said, "We're a fee only asset manager and we are a fiduciary," all that, that's all well and good, and there's some great people that do that.

But, just make no mistake. They're still selling the 1% management fee, but the problem is it puts the client in the position where they've got a little bit of doubt and they need to somehow watch out for the advice. Because, they know that, over time, it's going to require that they transact with this advisor for the advisor to get compensated for the time that they've invested, which

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either does one of two things.

Some advisors, that means to attract on a client, they only spend two meetings with them before the client implements because they're going to have a lot of clients say no, which means they never spend enough time with the client for the client to truly, deeply understand the decision that they're going to make. If they don't deeply understand the decision they're going to make, how likely is it that they're going to feel good about that decision for the long run? That's one way it can go.

The other way it can go is the advisor spends a truckload of time with the client and the client just feels nearly guilty and needs to transact, which also is not good. So, it gets away from the educational and coaching side, or for the client to feel like it's educational and coaching-based. When they have that question, they may ask, "Would I be better off building an investment portfolio with this advisor or buying real estate? Would I be better off buying index funds? Should I be putting money in my company 401(k) instead of with this advisor? And as each of those come up, what kind of life insurance should I have? What type should it be? How much should it be? Could I solve my estate tax issues with appropriate trust and estate planning, not just with life insurance?"

When all those questions bubble up, now the advisor is almost greeted with a little bit of I don't want to go quite as high as suspicion, but whatever in your mind would be slightly higher than that, let's just call it skepticism, in all of the recommendations that are made, because the client wonders, "Well, wait. It seems like every recommendation has to do with something that you put in our hands."

Then, along with that, there are key areas that now, because most of the advisors out there are compensated on the asset management or compensated on the product and there is no other way, there's no design fee being charged, what are the things that often get ignored, don't get looked at? Or, if they are looked at, only get lip service from that advisor. Well, that's the car and homeowner's insurance, the umbrella policies.

They don't really address whether or not their client has appropriate levels of disability insurance, and I, having worked with, coached advisors, worked to recruit advisors to our firm, I cannot tell you how often I have heard an advisor say, "Well, I'm a fiduciary. I put the client's interest first above all else, and that's why we only charge 1 or 1.5% a year fee." Yet, I'll ask that advisor, I'll say, "Well, do you do any insurance stuff for your client?" They go, "Yeah, we take care of some life insurance." I say, "How about disability insurance?"

The answer, inevitably, is, "That is a pain." That disability insurance is difficult to underwrite, it's the hardest type of insurance to get. So, we don't handle that because we don't want to risk upsetting our client with the outcomes that could be. So, I am a sometimes, not enormously abrasive, but I can be just abrasive enough, and I'll ask, I'll say, "Wait a second. You're the fiduciary when it comes to the way you invest for them, as you say, and the way you're charging them, you say, is all fiduciary standard. But then, when it's inconvenient for you to comment on it, or to take a solid look at it, or make recommendations on something like car insurance, homeowner's insurance, disability, you just sort of ignore it?"

As you might imagine, that doesn't really foster a fruitful conversation, which is why I don't say that anymore. But, it's real. That's a real issue. If we don't have somebody that's kind of standing next to us, with their financial knowledge, looking at everything that we're doing, helping us strategically pull it all together, then we oftentimes don't have somebody looking at our wills and trusts, our business agreements, our budgeting, or our tax strategy, whether or not our mortgage is correct.

That stuff, we don't do mortgages, we don't do car insurance, we don't do homeowner's insurance. We're not tax consultants. We don't file people's tax returns. You know what we do though, is we look at all of those things, sit back long enough with the client understanding the real intentions of what they want to do with their money, and then help them pull together the appropriate strategies from each of those experts to help them build the life that they want.

So, when we get into this design build model we're after rather than it being a sales-based model, which is the way I was raised up in the industry and the way many people have engaged the financial industry, and it's become so much that way that people really reflect. It's just that's the way it is. If your doctor treats you a certain way, that's just medicine. This is just how finance works, and what I'm going to tell you is there's a different way.

What we want you to do with our design and build model is that we sought to create a safe learning environment for our clients, allowing them to address common concerns, and then provide exceptional value for each of them so that they can engage in a process knowing that they can ask the questions that they want to ask, they can lay out the aims that they want to have for the future, and know that they've got somebody in their corner that's helping them design for those aims without needing to shape it inside of a product. If you've ever felt like, "Man, it feels like this advisor is really trying to put a square peg in a round hole," that could be why.

So, we separate those two, the design from the build, for that specific reason, because we want our clients to have a consultative approach when it comes to their money. So, we're going to be setting it up where when we take somebody through the design phase, there is a flat fee. There's just going to be a flat fee for engaging us. Effectively, we will take you through the design process that's going to be between four and six meetings, more than likely, over five to six weeks depending on scheduling, and we will do the design.

During that design, there may be things that have to be built, and when we hit those things, we're going to give our clients the options, "Do you want us to handle that, or do you have somebody else on your team that you want to handle that part for you?" and both are okay with us. Because, what we want to make sure that we can do is get you through that design phase quickly and then have us on retainer for the remainder of the year so that you know you're going to get the best advice possible because you paid for it.

Now, the next question is how do we set the fee? That's always an important question. People wonder or worry about that. Well, the way our process is working is that we first have a philosophy conversation with you. So, if you've not had a chance to understand our philosophy, I take time and I give away an hour of my time to simply say, "This is our philosophy. This is how we look at the financial world differently," and as a result of walking you through that conversation, at the end, there is no close. We're not coming after you. We're not going to say, "You know, do you really care about your future? Then, you should engage with us." No. We need that philosophy conversation to be a safe place so that every one of our clients feels comfortable introducing people.

So, the only thing that you get the opportunity to do at the end of that philosophy conversation is you can ask for an application. You can ask for an application. Now, if you want an application, then we send one to you, and it's okay. We are perfectly fine. If somebody's not in that wheelhouse that we normally work in in terms of household income, that's okay. We'll still send you an application and here's why. Because, the next meeting we're going to have is an assessment meeting, 30 minutes. And in that 30-minute meeting, what we're going to be doing is we're going to be taking time with someone to understand whether or not we're a good fit.

So, what are we going to look for? Well, first, how were they in going through the application. We're looking at we're going to engage with people for a minimum of a year. Though, my hope would be anyone we would engage, we would be building a lifelong relationship with. So, I really don't want to be working with anybody, our advisors don't want to be working with somebody that they don't feel good about in the early stages of the process: the person doesn't treat us well or they're not super friendly, or whatever. I mean, maybe not that much different than what you might do if you're hiring somebody to your team and your business. If they don't perform well in that first 90 days, that's probably a good indicator. We want that in the early stages of the process.

We're saying, "Are we going to like working with them," and then we're also looking for what's important to them about money? Is there a philosophy and cultural fit between us and the client. Because, are we going to feel good about helping that client build the future that they're after?

Then, lastly, we also have to ask ourselves the question, "Is it going to be ethical for us to charge this person the amount that we charge, which is not insubstantial, is it going to be appropriate for us to charge that much where this person is going to be really happy having paid the fee, or are we going to create a dissatisfied interaction, which is not what we want?"

We have different levels of that fee where it's a higher level fee, not surprisingly, to work with me, and that's a fee that is elevating over time, which is why I'm not putting it on the podcast because that can move up over time as we get busier and busier and continue to enhance that process. A lower fee to engage with one of our advisors, and then we also have a fee that is like an entry-level fee that would be purely for portfolio analysis. If we see that somebody doesn't really need the level of horsepower our full-on consulting and design process is but we can see they're significantly overpaying in fees in their portfolio, we can run an analysis to help them understand what that is and help them get an appropriate allocation for what they're doing with their portfolio.

So, those are the kind of three levels of engagement we currently offer. We'll set the fee based upon making sure that it's valuable enough for the client that we estimate they will be happy doing it as well as, will we be happy being in that engagement?

Now, one small note. Some of you listening may have even paid a financial advisor by the hour somehow, and there's a very specific reason why we did not do that, and it has to do with

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whether or not we create a relationship with the client that has the client willing to engage, educate themselves, and be coached? The problem is if we're taking $250 an hour, or $300 an hour, or $400 an hour to do that, then the question creeps back in and doubt can occur in the client's mind of, "Oh my gosh, this seems like it's taking a long time. How much am I paying for this?" and then what that causes is another degree of distrust between the advisor and client. That's why we're not doing the hourly consulting, because of that pitfall. We don't want our clients to have that. We want to have the coaching, educational relationship.

Now, why do we also do design and then offer the build. You can kind of picture those as two circles orbiting next to each other. Why do we have a design and build part of our process? It really goes back to things I used to tell jokes about to other advisors, and what I realized about three years ago is how bad it is.

You see, I used to have clients come in, and this has happened multiple times to me where a client comes in and shows me the financial plan they have. Maybe it's they paid somebody to "build the plan", and that plan was in a nice leather binder. It was a little dusty, and it had a dent in the top of it. I was like, "Can I ask you why this is dusty and it has a dent on the top of it?" and they say, "Well, this has been holding up the pool table outside on our covered patio. It wasn't real level, so we kind of crammed this underneath," and they had implemented none of what was in there.

So, we want to be able to be in the client's corner and working with them for the entire year even if they're not implementing with us, to make sure that they actually implement the very things that they envisioned would be important for them for the future. Because, if you haven't noticed, nearly everything in life without a relationship, without guidance, without coaching, nearly everything in life will draw us away from taking the time to build the future to meet the aims that we're after. Everything, every advertisement, every TV show, every chance to read a book or just take extra time with our children. And those are all good things, but they all distract us from our ability to take the time to be really, really effective by taking good care of our money and implementing the structures that need to be there for us in 5 years, 10 years, 15 years, 20 years, and 50 years.

I'm going to close on why 50 years. You see, we talk a lot about design and build a good life, and that's why we have now brought in this design and build process. Though, I want you to consider something. If you're married and healthy at age 65, and we don't have a single client who's under the age of 65 right now who had said that their goal is to be really sickly and unhealthy at age 65. So, our clients, 100%, want to be healthy when they're age 65.

If they are, then the current mortality statistics state the following is that one of them, so a couple of two, one of them has a 50% chance of outliving age 95 - 50% chance of outliving age 95. If you're healthy and alive at age 65, one of you is going to make it to age 95. That means it takes a lot of design. It takes a lot of work, and you can't sit back and not get educated about your finance. Because, if you're 45 right now, that means you have a 50-year planning horizon ahead of you.

If you want to get into multi-generational stuff: helping your children and grandchildren be financially responsible, and be prepared to receive whatever money you might leave behind, you may be dealing with a century ahead of you right now.

I'm so glad you guys could be with us today and that I could share with you a little bit about why we're making this shift to take better care of our current clients and our new clients that will be coming on board, and know that what we want to do with these podcasts is really focus on you, your family, and the knowledge that you need to help yourself design and build a good life.

Do not hesitate to reach out to us. You can reach us on the website. If there's a podcast you'd like to hear, shoot us an email at info@sfgwa.com, and if what you want is that philosophy conversation or a 10-minute financial triage call, give us a call. I'll take the time. If you're investing in yourself and the podcast and if I'm not available, one of our team will be sure to take some time with you to help you design and build a good life. Have a great rest of your day.

Hi, Paul Adams here. I want to acknowledge you for taking the time to invest in yourself by listening to our podcast. Not everybody does that, and out of my commitment to you, I will take just a few of our podcast listeners between each of our episodes and spend time with them one-on-one. And if you think you'd like some of that one-on-one time to learn more about our process, our philosophy, or whether or not we'd be a fit to work together, just email info@sfgwa.com - that's info@sfgwa.com - and I'll be more than honored to take that time with you. You can also go to our website, www.sfgwa.com, download the first three chapters of my book, see upcoming in-person events that we have, or listen to past episodes. You can also go to our Facebook page and engage us there, our LinkedIn, and send us questions for upcoming podcasts. You might hear one of your comments or questions on a future podcast. For our full disclosure, you can check the description on this podcast, or on the podcast series, or go to our website. Have a great day.

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