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Why work with a financial advisor

Financial planning can help you achieve your goals—and feel better too.

FIDELITY VIEWPOINTS – 02/27/2019

Financial planning Retirement Investing strategies Managing an inheritance Taxes Tax efficient investing Capital gains tax Charitable giving Wealth planning Health insurance 401(k) Financial Checkup Retirement accounts Charitable Planning Calculator Health Savings Account Financial Wellness Quiz IRA Insurance services Giving Account

Feedback

- Industry studies estimate that professional financial advice can add between 1.5% and 4% to portfolio returns over the long term, depending on the time period and how returns are calculated.[1]
- A one-on-one relationship with an advisor is not just about money management. A financial advisor can help provide ongoing financial planning so you can have peace of mind while pursuing your life goals.
- The financial planning process includes defining your goals, understanding your current situation, and identifying the key steps to move forward.
- Beyond long-term goals like retirement, and shorter-term ones like buying a house, education, or travel, holistic financial planning can also include legacy planning, family support, health care, insurance, and charitable giving.

When we make big decisions in life, most of us look for a source of expertise and guidance to help us make thoughtful choices to meet our individual goals and needs.

That's what professional financial advice is all about. Ongoing financial planning can pay off in many ways. Industry studies estimate that financial advice can add between 1.5% and 4% to account growth over extended periods.[1]

Of course, the value of advice varies greatly. For one thing, financial advice can mean very different things to different people. For some investors, online financial planning tools or a single investment solution may meet their needs. For others, including people with more wealth, complex situations, or those who put more value on having a personal advisor, a one-on-one relationship with a financial advisor may be a better fit. In addition, the value of financial advice will vary over different time periods, depending on the personal circumstances, market conditions, and more.

Feedback

For most investors who choose to work with an advisor, advice is not just about investments. More than half of all investors said that ongoing financial planning and coaching services were the most valuable part of their advisor relationship.

In this special report, we bring some aspects of an ongoing financial planning relationship to life through Sally and Ben, a hypothetical couple.

Sally & Ben
Age: 55
Savings and investments: $1,000,000
Income: $250,000 per year (total)
Goals: Support their son, maintain lifestyle during retirement, leave a legacy to a local charity

Plan

Everyone has goals and an advisor can work with you to understand those goals, model and quantify your options, confirm the steps you are taking and illustrate alternative plans to get you there. Over time, holistic planning may include retirement, housing, education, travel, family support, charity, and more.

Sally and Ben's financial planning

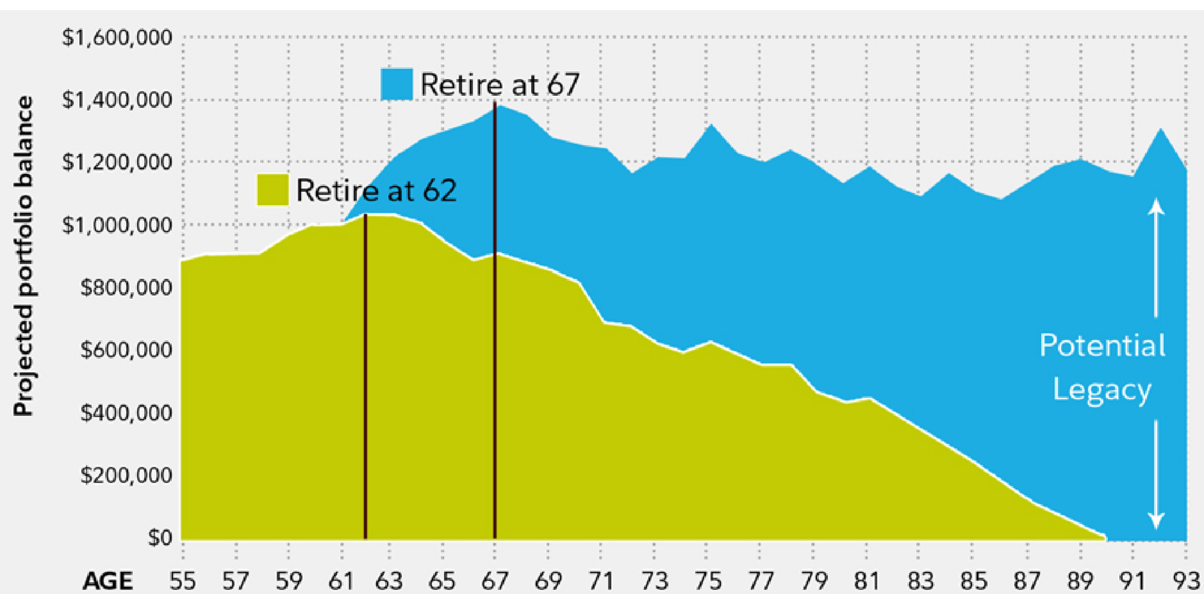
When Sally and Ben first met with their advisor, he coached them to focus their attention on their major goals—and where they stood on the road to realizing them. Sally and Ben were considering how to help their 24-year-old son, create income in retirement, and manage the impact of taxes. Their advisor worked with Sally and Ben to create a picture of their current financial situation, helping them pull together all needed documents and to develop a balance sheet. Sally and Ben and their advisor agreed to an agenda of items they would tackle as next steps.

At the next meeting they reviewed their balance sheet, beneficiary designations, asset allocation, and progress toward their goals. Their advisor used financial assumptions and the details of their situation to project their current cash flow and get a sense of their retirement planning.

During their initial conversation, they were surprised to discover that Sally wanted to retire with Ben at age 62 while Ben was expecting both to work until age 67. Ben and Sally learned, according to the hypothetical projections, that by retiring at age 62 there was about a 10% probability they could run out of money by 2052, when they'd be 89 years old. While that level of risk might have been acceptable to some, both Sally and Ben have a family history of long lives, and the couple wasn't comfortable with this risk that they would outlive their savings.

Instead, by waiting until age 67 to retire, they'd have more years of savings and compounded earnings, fewer years in retirement, and a higher Social Security benefit so the probability was higher that they could maintain their lifestyle, and have money left over.[2] Also, their hypothetical surplus meant their savings had the potential to last throughout their lives and, also, provide an inheritance for their son and a donation to Ben's favorite charity.

Retiring later can boost your retirement income security and more



Important: The projections or other information regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. Your results may vary. This hypothetical example illustrates the projected household portfolio balances in 2 different retirement age scenarios—retiring at 62 and retiring at 67 and planning to age 93. See footnote 2, "Retirement age," for important details. Source: Fidelity Investments.

Implement

Financial planning is beneficial only if you implement the advice. A good coach can help you put your planning into action, trying to help you avoid costly investing mistakes along the way. A financial advisor can help you choose an appropriate mix of investments, adjust your portfolio over time, and withdraw your savings in a tax-efficient way to help realize your goals.

Implementing Sally and Ben's financial plan

Sally and Ben already had a portfolio that made sense for their goals, risk tolerance, and situation. But where they save—and how they are charged and taxed—also matters. Working with their advisor, Sally and Ben looked at the benefits of a Roth IRA and health savings accounts (HSAs), and also wanted to understand the benefits of charitable planning. Based on that discussion, they decided to:

Convert some of their IRA savings to a Roth IRA. They will need to pay taxes on the IRA conversion, but potentially reduce taxes on withdrawals in retirement.

Try to make the most of their HSAs as a way to save by paying any medical costs out-of-pocket and investing the HSA money for growth.

Donating appreciated securities for charitable donations. By making a direct donation of $50,000 worth of stock that has appreciated $30,000, they could potentially avoid capital gains taxes—and increase the value of their federal income tax deduction from $15,858 to $18,500 (see chart).[3]

Donating appreciated assets may help reduce taxes and boost your charitable gift

Sell stock & donate cash proceeds		Donate stocks directly to charity
$20,000	Value of stock when purchased	$20,000
$50,000	Current price	$50,000
$7,140	Capital gains and Medicare surtax paid on $30,000 (23.8%)	$0
$42,860	Total contribution to charity (after deducting federal taxes)	$50,000
$15,858	Value of charitable tax deduction	$18,500
		Greater tax deduction Greater contribution

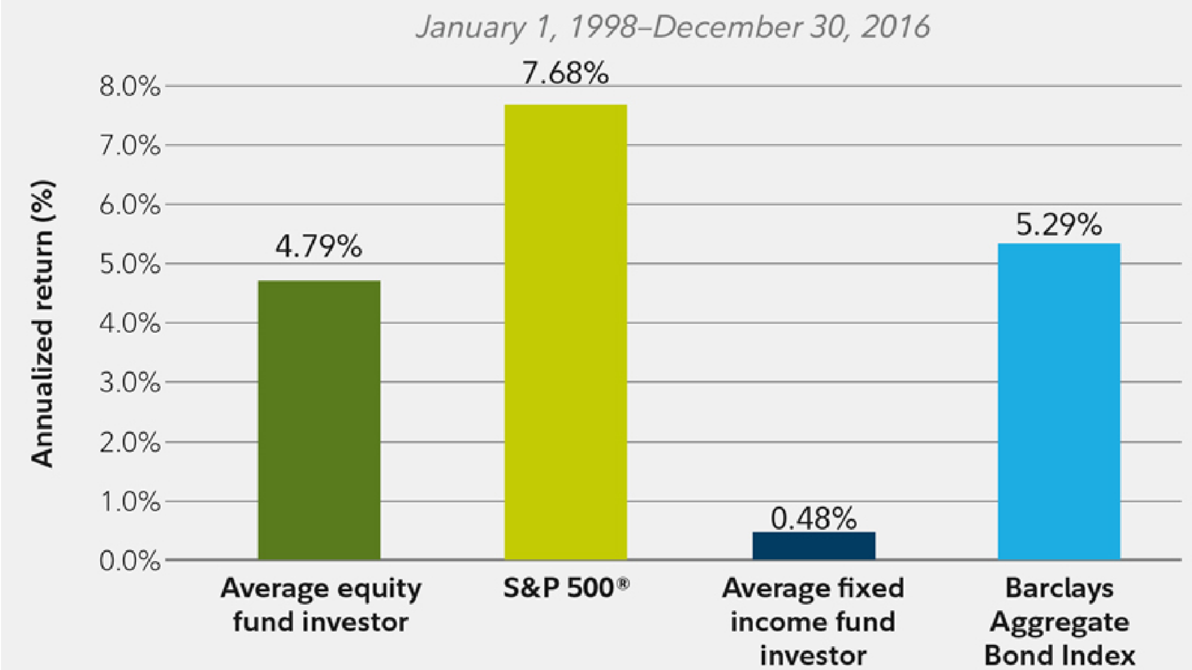
Source: Fidelity Investments. This is a hypothetical example for illustrative purposes only. The chart assumes that the donor is in the 37% federal income bracket with an adjusted gross income (AGI) of $500,000. Assumes all realized gains are subject to the maximum federal long-term capital gain tax rate of 20% and the Medicare surtax of 3.8%. Information herein is not legal or tax advice. See footnote 3, "Charitable donations," for more details.

Manage

Working with an advisor can provide a disciplined process for on-going financial planning, regular check-ins, portfolio reviews, and progress reports. An advisor can also help with updates to reflect new goals or life events, as well as manage risk and seize opportunities as markets or tax laws change.

A financial advisor can work for you through market ups and downs—and provide the guidance and encouragement you may need to stay on track to avoid the sometimes costly mistakes investors make during volatile markets.

Timing has caused investors to realize below market returns



Source: Quantitative Analysis of Investor Behavior 2016, DALBAR, Inc. **Past performance is not a guarantee of future results.** Data compares performance from January 1, 1998 to December 30, 2016. See footnote 4, "Investor behavior" for more details.

Market moves also create tax planning opportunities. Consider the potential of tax-loss harvesting to help lower capital gains taxes. The rules can be complex. But you can use realized capital losses to offset realized capital gains and, potentially, a small portion of ordinary income. Plus, unused losses can be "carried forward" and used in future years.

Here's how tax-loss harvesting could work for Sally and Ben. Say Sally is subject to a 20% long-term capital gains rate, so she would owe $2,000 in taxes on a $10,000 long-term capital gain this year. But what if she had sold $6,000 worth of stocks at a loss during the same year? Those losses could offset $6,000 worth of capital gains this year, leaving a $4,000 taxable capital gain, and only an $800 tax bill. That's a tax savings of $1,200 this year, increasing her after-tax gain by 15%.[5]

Of course, you never want tax considerations alone to drive your investment decisions. But if sale of both securities were in sync with your investment objectives, the tax savings would provide a boost to your after-tax return.

Tax-loss harvesting can help boost after-tax returns

	Without tax-loss harvesting	With tax-loss harvesting
Sell an appreciated stock for a gain	$10,000	$10,000
Sell stocks for a loss	$0	–$6,000
Total taxable gain	$10,000	$4,000
Taxes owed at 20% rate	$2,000	$800
After-tax gain	**$8,000**	**$9,200**

Source: Fidelity Investments. For illustrative purposes only. Does not consider state taxes. Capital gains taxes are hypothetical and reflect a 20% capital gains tax and assume that the investment decisions are in accordance with wash sale rules. See footnote 5, "Tax-loss harvesting," for details.

Feedback

Managing Sally and Ben's plan

Each year, Sally and Ben plan to have 2 check-ins with their advisor. During those sessions they'll review any major changes to their goals or life. So, for example, if Sally has to stop working early due to health issues, or Ben's mother leaves them an inheritance, their planning could incorporate the changes. During their check-ins, they'll review their portfolio to help ensure it's still in line with their goals and identify opportunities for tax-loss harvesting and other tax-smart strategies.

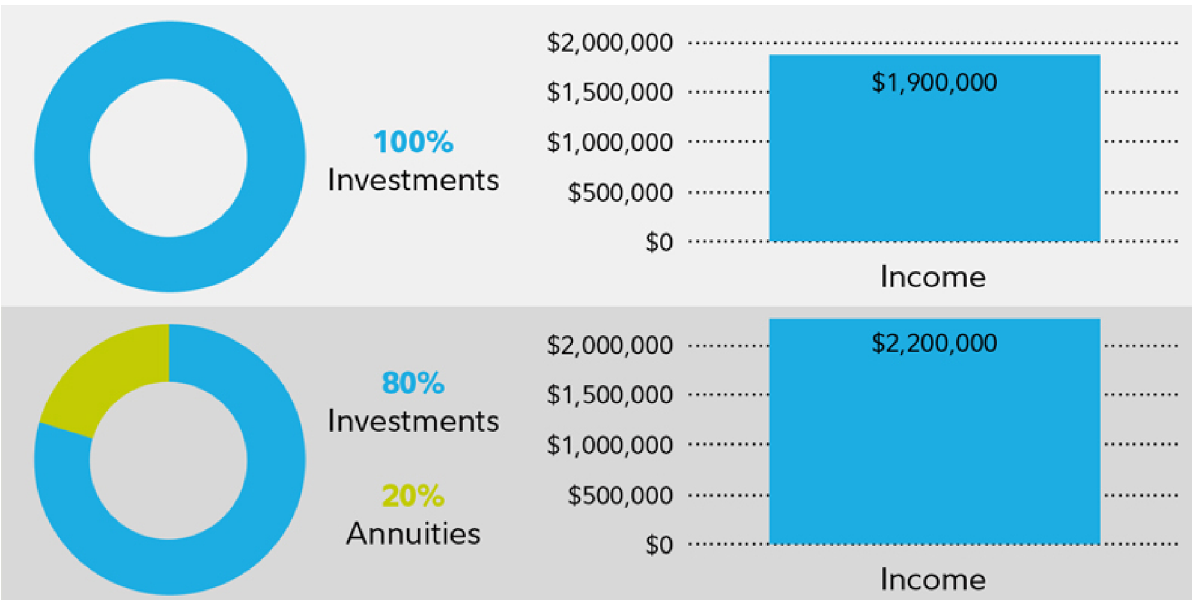
Currently, they are wondering if they need to make changes to their portfolio or incorporate different income solutions as they near retirement, including whether to annuitize a portion of their retirement savings.

To help them decide, their advisor provides a hypothetical example, assuming Sally and Ben are now 67 years old and about to retire with $1 million in investments. Going forward, they will be living off their nest egg, and no longer saving. They are looking to their advisor to help them evaluate their retirement expenses and income sources, identify any gaps, and potentially save taxes along the way.

The advisor lays out 2 scenarios. In one, Sally and Ben shift all of their savings to a more conservative mix of 50% equity, 40% bonds, and 10% cash—a common asset mix for retirees—and use withdrawals to cover essential and discretionary expenses in retirement. In the other, they put 20% of their savings in a guaranteed income annuity that along with Social Security will cover their essential expenses, and the rest in that 50-40-10 asset mix. Because they will be able to cover essential expenses with Social Security and the annuity, they can invest the rest of their portfolio for a longer period. Also, the annuity provides some longevity protection for Sally and Ben. Of course, they will want to pick their annuity provider carefully as guarantees are subject to the claims-paying ability of the issuing insurance company.

If they live until age 93, the second strategy could hypothetically produce more lifetime income, with little concern about running out of money because their essential expenses are covered by Social Security and the annuity.[5]

See what a $1 million investment could generate in income over 26 years in retirement

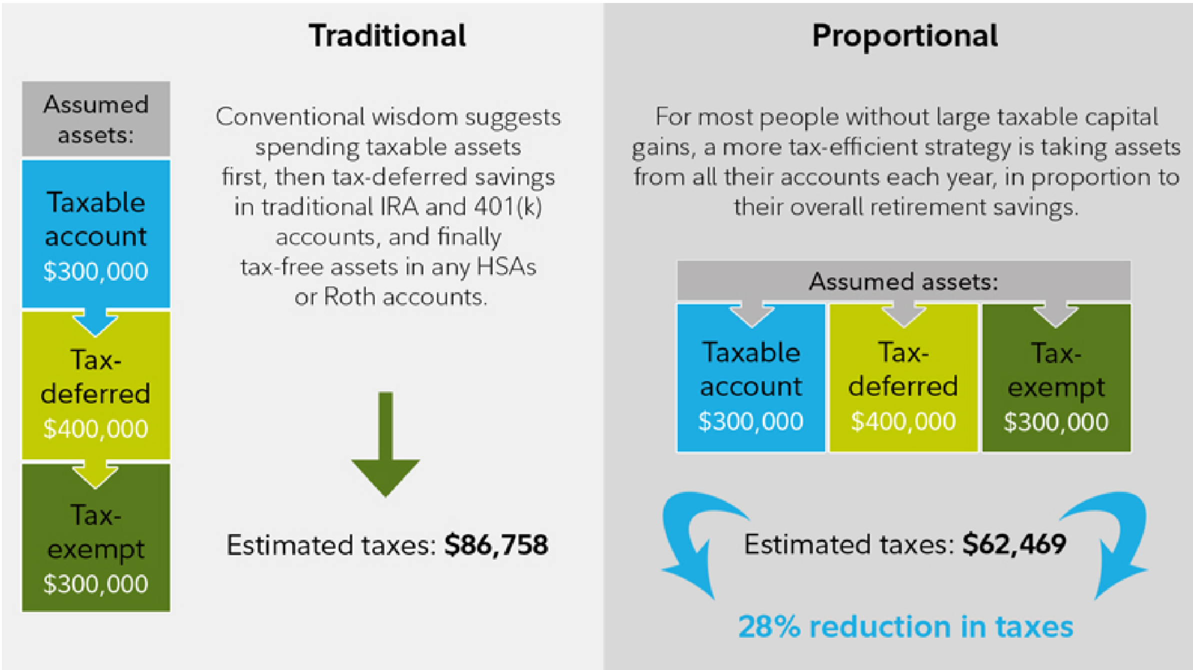


Important: The projections or other information regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. Your results may vary. This hypothetical example illustrates the projected life household income and ending balance for $1 million portfolio both with and without an annuity. Please see footnote 6, "Retirement income," for more details. Source: Fidelity Investments.

There are also tax-smart strategies for withdrawing money in retirement that could potentially help reduce Sally and Ben's taxes and extend the life of their retirement savings. Some people believe that taxable assets should be spent first, then tax-deferred savings in traditional IRA and 401(k) accounts, and finally tax-free assets in any Roth or HSA accounts. But that is not always the best approach when it comes to your federal income taxes throughout retirement.

In general, for some people without relatively large taxable capital gains, a more tax-efficient strategy may be taking assets from all their account types each year, in proportion to their overall retirement savings. Let's assume that by retirement at age 67 Sally and Ben have $400,000 in tax-deferred IRA assets, $300,000 in a tax-free Roth account, and $300,000 in a taxable brokerage account. Taking a proportional approach to withdrawals during retirement could potentially reduce the taxes they pay on that money by an estimated $24,289 or 28%.[7]

Smart withdrawals may help reduce federal income taxes in retirement



Source: Fidelity Investments. Hypothetical example.

The bottom line

Financial advice is more than just numbers and investments. It's a process that can help you make a plan, chart your progress, and hopefully achieve your personal and financial goals—while feeling more confident along the way.

The financial planning checklist

An advisor can help you get started building a plan to reach your goals.

- Identify or discuss your personal and financial goals.
- Evaluate whether you're on track to meet your goal(s).
- Determine the following:
  - Is your spending and cash flow appropriate?
  - What does financial protection mean to you, and how important is it?
  - What does growth mean to you, and how important is it?
  - Are your investments aligned with your preferences?
  - How will you manage your investment portfolio?

Implement your financial planning with the appropriate mix of investments to balance your financial needs and investment priorities.

Set up regular reviews to help refine your financial planning when there are changes in your lifestyle and personal situation.

Next steps to consider

Feedback

-

Connect with an advisor

Call or visit to set up an appointment.

-

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1. Value of advice sources: Envestnet, Capital Sigma: The Return on Advice (estimates advisor value add at an average of 3% per year), 2016; Russell Investments, 2017 Value of a Financial Advisor Update estimates value add at more than 4% per year); Vanguard, Putting a Value on Your Value: Quantifying Vanguard Advisor's Alpha® 2016, (estimates lifetime value add at an average of 3%); Morningstar Investment Management, The Value of a Gamma-Efficient Portfolio, 2017, (estimates value add for a subset of the service identified in this paper at an average of 1.5% per year). The methodologies for these studies vary greatly. In the Envestnet and Russell studies, the paper sought to identify the absolute value of a set of services, while the Vanguard and Morningstar studies compared expected impact of advisor practices to a hypothetical base case scenario. Please follow the links above to see important differences in the methodologies of these various studies.

2. Retirement age: This hypothetical example illustrates the projected household portfolio balances in 2 different retirement age scenarios—retiring at 62 and retiring at 67. In both cases the plan was designed to meet retirement income needs to age 93. The retirement at 62 scenario assumes household makes no further retirement contribution, immediately starts withdrawing from the hypothetical portfolio, and claims Social Security at a reduced amount at 62. The 67 scenario assumes the household makes 15% contribution to the hypothetical portfolio until 67, then starts withdrawing $7,000 monthly from it, and claims full amount of Social Security at age 67. Legacy indicates any surplus that remains in the hypothetical portfolio at the end of plan horizon of 93, having withdrawn $7,000 a month to fulfill retirement essential expense requirement.

The projected portfolio ending balances shows the hypothetical outcome created using historical data to run multiple simulations for the hypothetical index portfolio in a wide range of market conditions. These results show a "weak market," meaning the 90th percentile of market scenarios. Planning for the 90th percentile of market conditions is considered a "strong plan" in Fidelity's retirement planning tools. In other words, this analysis looked at several thousand potential scenarios, and in 9 out of 10 market scenarios the hypothetical portfolio performed at least as well, while 1 out of 10 times the portfolio failed to perform as well.

The calculation assumes a level of diversity within each asset class consistent with a specific market index. Volatility of the stocks, bonds and short-term asset classes is based on the historical annual data from 1926 through the most recent year-end data available from Ibbotson Associates, Inc. Stocks (domestic and foreign), bonds, and short-term are represented by S&P 500®, U.S. Intermediate Term Government Bonds, and 30-day US Treasury bill, respectively. Annual returns assume the reinvestment of interest and dividends, no transaction costs, and no management or servicing fees. It is not possible to invest directly in an index. All indices include reinvestment of dividends and interest income.

3. Charitable donations: This is a hypothetical example for illustrative purposes only. The chart assumes that the donor is in the 37% federal income bracket with an adjusted gross income (AGI) of $500,000, and all realized gains are subject to the maximum federal long-term capital gain tax rate of 20% and the Medicare surtax of 3.8%. State and local taxes, the federal alternative minimum tax, and limitations to itemized deductions applicable to taxpayers in higher-income brackets are not taken into account. Please consult your tax advisor regarding your specific legal and tax situation. Information herein is not legal or tax advice.

4. Investor behavior: The Quantitative Analysis of investor Behavior (QAIB), 2016, was produced by DALBAR, Inc. The QAIB uses data from the Investment Company Institute (ICI), Standard & Poor's, Bloomberg Barclays Indices, and proprietary sourced to compare mutual fund investor returns to an appropriate set of benchmarks. Covering the period from January 1, 1998 to December 30, 2016 the study utilizes mutual fund sales, redemptions, and exchanges each month as the measure of investor behavior. These behaviors reflect the "average investor." Based on this behavior the analysis calculates the "average investor return" for various periods. These results are then compared to the returns of respective indexes. QAIB calculates investor returns as the change in assets, after excluding sales, redemptions, and exchanges. This method of calculations captures realized and unrealized capital gains, dividends, interest, trading costs, sales charges, fees, expenses, and any other costs. After calculating investor returns in dollar terms, two percentages are calculated, total investor return rate for the period and annualized investor return rates. Total return rate is determined by calculating the investor return dollars as a performance of the net assets, sales, redemptions, and exchanges for the period. Annualized return rate is calculated as the uniform rate that can be compounded annually for the period under consideration to produce the investor return dollars. The S&P 500 is a market capitalization-weighted index of 500 common stocks chosen for market size, liquidity, and industry group representation. S&P and S&P 500 are registered service marks of Standard & Poor's Financial Services LLC. The Barclays Aggregate Bond Index is an unmanaged market value-weighted index representing securities that are SEC registered, taxable, and dollar-denominated. This index covers the US investment-grade fixed-rate bond market, with index components for a combination of the Barclays government and corporate securities, mortgage-backed pass-through securities, and asset-backed securities. Indexes do not take into account the fees and expenses associated with investing, and it is not possible to invest directly in an index.

Feedback

5. Tax loss harvesting: Capital gains taxes are hypothetical and reflect a 20% capital gains tax and assume that the investment decisions are in accordance with wash sale rules.

6. Retirement income:
This hypothetical example illustrates the projected household portfolio ending balances and incomes in 2 different scenarios: with and without acquiring an annuity. The first scenario assumes the $1 million account is fully invested to a balanced asset allocation, which contains 50% stock, 40% bond and 10% short-term. The second scenario assumes household takes out $200,000 from $1 million to purchase an annuity, and the rest is invested to a balanced asset allocation. The household is assumed to withdraw $7,000 each month to cover essential expense needs until the end of age 93. Legacy indicates any surplus that remains in the hypothetical portfolio at the end of plan horizon of 93, having withdrawn $7,000 a month to fulfill retirement essential expense requirement.

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7. Withdrawal hierarchy: This hypothetical illustration is created assuming a household with a combined total asset of $1,000,000 across tax-deferred, tax-exempt and taxable accounts. The household is assumed to consume $60,000 annually. Investment return is assumed to be a fixed 5% annual rate during the entirety of retirement. The hierarchy withdrawal method indicates that the household withdraws from the specified account until completely deplete that account, and subsequently move to withdrawing solely from the next account. Pro-rata withdrawal method indicates that the household withdraw proportionately to the balances across accounts every year to fulfill its withdrawal goal. The efficacy is measured by number of years the total household portfolio can last while supporting its annual expense goal. 2018 tax brackets are used and all values shown are in real dollars.

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