New tricks for an old salt

Paying an upfront fee-for-advice has drawn John Miller infinitely closer to his adviser, as Mark Story discovers.

To Adelaide-based radiologist John Miller paying trailing commissions instead of up-front fees for advice is akin to paying for the privilege of a public hospital bed instead of having your own suite in a private hospital ─ for less money. He's adamant the transition to a full fee-for-advice service three years ago delivered a dramatic improvement in the relationship with his professional planner, Travis Hutchinson of Godfrey Pembroke Financial Consultants. "I really feel like Travis is working for me and that I'm getter better advice, and more of it," says Miller.

To Miller the act of paying Hutchinson an upfront fee, instead of the product provider paying him makes Hutchinson somehow more accountable for delivering successful outcomes. Their paths crossed three years ago when Miller went in search of a financial planner to convert a couple of legacy super policies he'd originally taken out in semi-retirement back in 1994 to allocated annuities.

He became quickly disillusioned when a large financial planning firm proposed to sock him 5% of his entire portfolio's net-worth up-front in annual fees. Ironically, when Godfrey Pembroke Financial Consultants offered to charge him 0.6% to perform the same exercise, Miller thought he was getting off lightly.

Having assumed that commissions were the norm and that everybody paid them, Miller didn't really give the matter much thought, even though he admits to not really understanding how they worked. "You don't see the trailing commissions come out so it's not really up-front and transparent," says Miller.

Having picked up on his dissatisfaction with a commission structure, Hutchinson replaced the $6,000 Miller was paying annually in trailing commissions with a $4,400 fee paid quarterly.

Primary objective

Like many self-employed 'veterans', Miller who's now well into his 70s saw property as his main retirement nest-egg. In addition to his super policies the only other assets he owned were the two residential properties he'd bought on the Gold Coast and in Adelaide's beachside suburb of Glenelg in the 1980s. He was also sitting on a substantial amount of cash that he'd parked in fixed interest since selling the medical centre he'd built and owned three years earlier.

In addition to altering the allocated annuities as required, Hutchinson was also charged with gradually moving Miller's fixed interest into direct equity exposure. While Miller's investment horizons are understandably wired to capital preservation and income, he has an unusually large appetite for equities for a man approaching four score years. That’s why Hutchinson set about developing a balanced portfolio of ‘safe’, blue-chip stocks displaying strong dividend yields.

What worked?

Attributable more to dumb luck than insider knowledge, the two residential properties Miller bought back in the 1980s have both come up trumps having delivered income while appreciating in value many times over. To the extent that they offer both capital growth and (all important) tax-free income, Miller says his direct equities strategy is proving equally successful.

While there aren’t too many skeletons in Miller’s investment closet he remembers getting his fingers burnt with the small parcel of shares he bought in a failed resort some years ago. Beyond that, his only other serious disappointment was with bonds (in the mid 1990s) which he claims contributed largely to a decade of under-performing annuities delivering returns of between 3.9% and 5%.

At Hutchinson’s instigation two older-style allocated annuities in ANZ and Macquarie were rolled over into a better performing MLC MasterKey fund. But performance aside, Miller says their ability to rebate trailing commissions in advance also meant he could move to an entirely fee-for-service structure.

Miller says having Hutchinson to act as conduit during the roll-over was an absolute blessing, especially when no one knew where a substantial sum had gone to for over a week. Considering the nightmares he experienced dealing with Macquarie and ANZ staff when changing policies, Miller was glad Hutchinson was there to take over. “Not knowing the whereabouts of $200,000 was an uncomfortable feeling. I should have been able to liaise with these financial institutions myself. But from my experience customer service people within these large firms are prone to give incorrect information,” laments Miller.

Value for money

Given that Miller is a self-confessed novice when it comes to shares, he’s confident with Hutchinson’s recommendations. Having bought a parcel of shares (worth between $25,000 to $50,000) on average every week for the last three years Miller has acquired a diversified portfolio of shares. But he says the execution of share trading could have been smoother. “I’d typically get a note advising that Travis’s sharebroker, who happens to be in Queensland required payment within three working days. In hindsight, I should have asked him to explain this arrangement in more detail,” says Miller.

Beyond that, he can’t find too much to fault with his relationship with Hutchinson. In addition to their quarterly meetings, Hutchinson is in regular phone contact. He also provides reports confirming any investment decisions that have been made and gains Miller’s sign-off before they’re acted upon. “Compared to year’s passed when I was almost frightened to ring my adviser, I feel that Hutchinson is working directly for me," Miller says. "The act of paying him an up-front fee makes him more accountable to me as the client."

Miller

Portfolio snapshot

Property: Adelaide, SA: Purchased in 1986, up almost 400% in value.
Gold Coast, Qld: Purchased in 1983, up 300% in value.

Managed funds
Domestic: MLC MasterKey Allocated Pension
Domestic: Macquarie Allocated Pension

Shares
Direct exposure to around 20 ASX-listed shares: Predominately blue-chip, high yield stocks.

The planner
Travis Hutchinson

Godfrey Pembroke Financial Consultants
Adelaide, SA

Hutchinson holds a Diploma of Financial Planning from Deacon University and is a Certified Financial Planner (CFP). After qualifying as a financial planner in 1998, he spent a year with National Mutual before moving to Deutsche Financial Planning, Deutsche Financial Planning was subsequently merged into Godfrey Pembroke in 2001.

Advice structure

When his former adviser retired a few years ago, Hutchinson gravitated from Miller's secondary to primary point of contact. As part of that transition, Hutchinson, at his request promptly moved Miller from a commission-based to a full fee-for-advice service.
Two of Miller's three allocated annuities (Macquarie and ANZ) were unable to rebate the trailing commission (in advance). As a result, Hutchinson decided to invoice him for the full $4,400 annual fee and rebate the trailing commission after the event. "Rolling over those legacy-style products meant we could provide the same level of asset allocation breakout without the trailing commissions," says Hutchinson.

History

Miller’s interest in moving to a fee-for-service structure was spurred by his realisation that it was Godfrey Pembroke and not him that was in control of commission payments. That’s why Hutchinson wanted to move him to a structure where they didn’t have to manually rebate any commissions.

Strategy

Given his age and appetite for risk, Hutchinson says dramatic changes to Miller’s investment strategy were unnecessary. The underlying rationale, says Hutchinson was to increase the tax efficiency of Miller’s portfolio through hybrid securities, Australian shares (with fully franked dividends), property securities and infrastructure stocks (like Babcock and Brown and Transurban) that offer high levels of tax-deferred income.

Due to Miller’s rental and fixed interest income, Hutchinson had little doubt he could significantly improve his tax profile. Given his investment appetite was pretty robust, Hutchinson started Miller on a programme of directly acquiring listed shares and hybrid securities.

“My recommendation was a combination of capital growth and fully franked dividend yields of between 4-5%,” says Hutchinson.

Having already reached the desired level of equity exposure, he says future share buying remains very much price dependent. He’s now looking to reinvest in fixed interest on a risk-adjusted basis.

“Given interest rates are likely to rise again, we may also look at hybrid listed securities with a floating coupon.”

Cross-generational

Given Miller had reached the stage where income was no longer an issue, his appetite for equities complemented a desire to buy assets that promoted cross-generational wealth. Miller’s appetite for asset acquisition gave Hutchinson the ability to deliver capital growth instead of just providing income.

Since 2006 Miller’s received around 10% net return annually, plus good capital gains. Prior to 2006 Hutchinson says the average 5.5% net return on allocated annuities was disappointing, especially given their limited capital growth upside.

Ideally Hutchinson would love to restructure the tax profile of Miller’s pensions and allocated annuities, but due to his age there’s no opportunity to ‘withdraw and recommence’. “We could cash-out the pension assets and buy more equities within the family trust. But given it’s in a tax-free investment structure this doesn’t stack up,” explains Hutchinson. “And because he’s over 75 he’s unable to recontribute to super beyond the 9% mandated contributions.”

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