professional PLANNER

When bad advice is worse than no advice

Written by Mark Story

29 JULY 2008

When bad advice is worse than no advice

It's scary to think that investors can fork out good money for financial advice year after year and yet remain blissfully lacking in even the most basic financial knowledge. But that's exactly the situation that NSW mid- North Coast widow Carol Moxen (not her real name) found herself in and which led her to replace her then financial adviser, who seemed oblivious to basic strategies for her retirement income. When Moxen's husband died unexpectedly five years ago, her only asset was the (freehold) family home.

With two grown-up kids off her hands,Moxen was able to manage on the income she received from her part-time property maintenance business.But like many self-employed people, she had never bothered to take out personal superannuation. Based on the advice of Moxen's forme radviser, the entire $400,000 she received as an insurance payout following her husband's death was spread between a dozen direct Australian equities (outside super)."It never occurred to me that I needed to be able to second-guess whether this recommendation was a good one or not," Moxen says. "In fairness, there would have been more scrutiny had I needed income-bearing assets to live on at the time."

Portfolio Snapshot:
Carol Moxen

Managed funds (superannuation):
BT Super Wrap, valued at $220,000, comprising:

Australian shares: Ausbil, Barclays, BT.

International: BT Core Global, BT Asian Growth, Trilogy International Growth, MSF Global Hedged Fund, Premium China Fund, Zurich Global Thematic Fund.

Property: BT Combined Property.

Australian Fixed Interest: AMP Enhanced Yield, Macquarie Enhanced Yield, Schroder Hybrid Securities.

Cash: At call, BT Institutional Enhanced Cash.

Allocated pension: $80,000 in the BT Super Wrap pension plan.

While the former adviser chastised her for progressively selling down around $50,000 in shares to renovate and buy another car, no efforts were made to help minimise her capital gains tax (CGT) bill. Sensing that Moxen could fare a lot better in the financial advice stakes - especially when you looked at the $4500 a year she was paying in fees – a friend eventually suggested that Moxen call her long-standing financial planner, Kristi Moy.

Back on track

Not too far into the review process, Moy realised that Moxen was bereft of any comprehensive retirement strategy, despite having paid for financial advice. Moy says that, not unlike most of her client base, Moxen was an unsophisticated investor whose trust in an investment adviser, allegedly acting in her best interests, was alarmingly misplaced. "It's unbelievable tothink someone can pay a large annual fee for so-called professional advice only to be treated with a cavalier approach bordering on contempt," says Moy. "But it happens every day and, unfortunately, many ill-informed seniors are seen as easy prey."

Transition to retirement

As Moxen's exposure to shares had provided neither income nor capital growth, Moy's first recommendation was to implement a transition to-retirement strategy. That meant selling down Moxen's share portfolio and placing the entire amount within personal super using a BT Super Wrap platform."We wanted to smooth out Carol's market exposures with less volatility. While it could be two years before current markets correct, this won't affect her income in the interim," advises Moy. "Given Carol's age [60], we also wanted to establish a portfolio that was sufficiently diversified to provide exposure to longer-term capital growth, and early this year we increased offshore exposures."

To minimise Moxen's liability for CGT, an initial $220,000invested within a BT Super Wrap was retained in the "accumulation phase". The net effect of the old pre-July 2007 rules meant only $83,000 of her capital gains were taxable, at the lower tax rate of 15 per cent. The remaining $80,000firstly went into super and was then immediately diverted to an allocated pension under a BT Super Wrap pension plan. **Entitlements**

As Moxen also wanted to stop working and devote more time to the

roses in her large English country garden, and her grandchildren, it was equally important that Moy construct an investment strategy that would maximise her regular income by preserving her Centre link entitlements. Unbeknown to Moxen (as someone born prior to July 1955), she was able to claim a widow allowance under Centrelink regulations, even after declaring her holdings within super. Asa single person with no dependents, Moxen is able to maintain her allocated pension (up to the value of $166,750) and still receive $472.80 per fortnight from Centre link. But if she has other fortnightly income of between $62 and$250, this reduces the fortnightly allowance by 50 cents in the dollar.

The Planner

Kristi Moy

Magnitude Financial Planning Forster, NSW

Moy holds a Diploma in Financial Services, has completed additional study in selfmanaged superannuation and estate planning and is an affiliate practitioner member of the Financial Planning Association (FPA). A former paraplanner within a large corporate bank, Moy has been in the financial services industry since 1996. Moy has been an employee of Mid North Coast Financial Planning on NSW's Mid North Coast since 2005. And as an authorised representative of Magnitude Financial Planning, she receives support from a national financial planning network.

ADVICE STRUCTURE Operating under a hybrid fee and commission structure, Moy lets her 180 clients - comprising SMSFs, individuals, couples and family trusts - decide which option best suits their unique requirements. Having witnessed most of the flaws associated with commission-based structures while working within other financial institutions, she concluded that companies operating under a fee-for-service model were more likely to retain clients over the longer term.

History Moy was referred to Moxen by one of Moy's clients early in 2006. The net effect of her long-standing financial adviser's unwillingness to provide even the most basic financial advice following her husband's death left Moxen financially illiterate. It was dissatisfaction with paying an annual fee for her planner to sit on the same bluechip stocks, while having to chase him for advice, that spurred Moxen's search for a value-for-money alternative service.

Strategy Early in Moy's review process it became clear Moxen had no underlying investment strategy. Moy's recommendations centered on restructuring Moxen's over-exposure to an inappropriate asset class (direct equities) recommended by her former adviser. That meant identifying and implementing the best all-round transition-to-retirement strategy through an appropriate tax vehicle (superannuation) that would best complement her need for regular income and capital preservation. Moy maximised Moxen's fixed income through an allocated pension while maintaining her (previously unclaimed) Centrelink entitlements and providing ongoing exposure to capital growth upside via a diversified range of managed funds (prior to her reaching age 65)

For income above $250 per fortnight, the fortnightly allowance reduces by 60 cents in the dollar. Centrelink entitlements, together with the allocated pension, meant that Moy was able to ensure Moxen achieved the minimum $25,000 she was looking for in annual fixed income. This income will increase once the remaining ($220,000) of Moxen's super funds are finally rolled over into the allocated pension. Moy says while many financial advisers don't want to sully their hands playing in the Centrelink sandpit, they often forget that for many retirees, these additional entitlements make a world of difference to their regular income. “Centrelink regulations are not for novices. Financial planners need to know their way around these sorts of entitlements to do the right thing by their clients,” Moy says.

Legacy

Another financial planning area where Moxen’s former adviser had left her in the dark was estate planning. As Moxen was still working part-time when she first approached Moy, it was important that her assets be protected from both potential predators and creditors. At Moy’s recommendation, Moxen was referred to an estate planning specialist to establish a testamentary trust that protected her two grown-up children as her primary beneficiaries.

Staying vigilant

In retrospect, Moxen shares the blame with her former adviser for not being sufficiently vigilant over her investment strategy. With the luxury of hindsight, she says her biggest mistake was giving him the impression that everything was running swimmingly when she clearly had insufficient knowledge to make that judgment call. “I know now that I sold myself short by agreeing to annual reviews that amounted to little more than10-minute phone conversations,” Moxen says. If she’s learnt anything since working with Moy, it’s the importance of keeping on top of her investment strategy through regular contact. “It’s fair and reasonable to expect a certain standard of service for the fees I’m paying,” she says.

Sadly, Moxen says, a lot of people, especially seniors,take the trust they place in their adviser so much for granted that they virtually abrogate responsibility by default. “You simply can’t assume that because you’re paying thousands of dollars in annual fees that an adviser will necessarily do the right thing by you,” says Moxen. While her portfolio is down marginally (0.31 per cent) since inception, Moxen says she’d be significantly worse off had she stayed in Australian equities, especially with the market 1000 points down on its November high of around 6400 points. She expects her diversified funds to quickly rebound once the markets finally correct. “I do trust Kristi implicitly to act in my best interests,” Moxen says.

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