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Three Key Investment Strategies Hidden in Plain Sight

Plain Sight Strategy #3: Controlling Costs

In the first two installments of our three-part "hidden in plain sight" investment strategy series, we've covered the importance of staying invested to earn market returns, while managing the risks involved. We'll conclude with what may be the most obvious and powerful advice of all, even if it does not seem to receive the attention it deserves.

1. Being there
2. Managing for market risks
3. Controlling costs

Don't spend more than you need to. Why do investors spend more than they need to on their investments?

Revealing the Numbers

While spending less to earn more seems obvious, the costs themselves aren't nearly as apparent. Disclosure requirements exist in most developed countries, but too often, the focus seems to remain on adhering to the letter rather than the spirit of the laws.

The issue does not just affect individual investors either. The California Public Employees' Retirement System (CalPERS) is currently the largest U.S. public pension fund, with nearly $300 billion in assets as of September 1, 2015.

In 2015, it embarked on an aggressive campaign to cut costs by seeking to eliminate its most fee-intensive money managers. According to a *Pensions & Investments* report, CalPERS officials "concede[d] they have been unable to determine just how much they do pay."

Crunching the Numbers

Adding to the challenge, many investors don't realize how seemingly modest costs can lead to significantly different outcomes over time. For example, this Securities and Exchange Commission (SEC) Investor Bulletin illustrates how a $100,000 investment earning 4 percent annually over 20 years would accumulate $220,000. If you calculate the earning power lost by removing instead of reinvesting a modest 0.25% annual expense, which is in the typical range for a low-cost index fund, you sacrifice about $10,000. Bump that to the 1% annual expenses (or higher) that are often found in higher-cost, actively managed funds, and you're giving up closer to $40,000.

Demanding the Numbers

Financial professionals and investors alike should insist on clarity wherever it seems lacking. As Vanguard founder Jack Bogle describes in this CNBC article, "If you had a crowd of investors who said, 'Look, this is just wrong,' [fund company] directors would have to listen, whether they want to know or not."

Instead, there is considerable evidence that, even when investors should be credulous consumers, they seem unwilling to question the costs. As expressed in a 2015 North American Securities Administrators Association (NASAA) report, "While broker-dealers may be complying with the technical requirements governing fee disclosures, our research shows that improvements are needed to raise awareness among investors of the costs associated with their brokerage accounts."

The NASAA report was based on a survey that found widespread confusion among investors. The report concluded: "Brokerage firms routinely charge fees to serve and maintain brokerage accounts, yet nearly one-third (30 percent) of investors said their firm had no such charges and one-quarter (25 percent) indicated they did not know whether they were being charged." Of those who did know there were fees involved, more than half did not know the amounts.

In short, the first step in managing investment expenses is to know what they are. Here, we offer an overview.

Trading costs: When you buy or sell funds, stocks, bonds or other securities, you pay a broker a commission to place your trade. These commissions are typically disclosed in your custodian's trade confirmation statements.

Fund management costs: If you are investing in funds versus individual stocks and bonds, you'll pay the fund company that manages them. These costs typically appear in expense ratio disclosures in a fund's prospectus or listed as an expense percentage by looking up the fund's ticker symbol on any number of online services such as Morningstar, Yahoo Finance and many others.

Administrative oversight: If you are invested beyond the pale of an individual brokerage account containing funds or securities, expect added costs to compensate for the extra administrative oversight and infrastructure involved. Think retirement plans, separately managed accounts, annuities, hedge funds, Real Estate Investment Trusts (REITs), private equity ventures, and so on. This is a key area where hidden costs can fester. As a result, investors often fail to realize there are added costs involved at all, let alone the extent to which they may exist.

As an investor, you deserve full disclosures and clear explanations, so you can determine for yourself whether the costs are justified. If we could offer only one piece of advice on the matter, we would conclude by urging you to forever heed this familiar adage: *If it sounds too good to be true, it probably is.*

Until next time, no regrets!

David Bromelkamp
President and CEO

FINANCIAL PLANNING TIP

How to Avoid a Conservatorship

Britney Spears' conservatorship has received a lot of attention by the press, as has the Netflix movie, "I Care a Lot." Both are situations where the conservatee alleges they are being mistreated and taken advantage of by the conservator.

A conservatorship is the appointment by a judge of a conservator to manage the financial affairs of another person due to old age or the lack of mental or physical capacity. The conservator may be only of the "estate" (financial affairs) or may also be of the "person" where the conservator takes charge of overseeing the daily activities such as health care or living arrangements of the conservatee (or ward).

Most times the conservator acts in a manner that is in the best interest of the conservatee. However, picture a situation where the conservator gets complete control over the ward's body and property, and they don't have the individual's best interest at heart. Very scary indeed. As a conservatee, you are deemed to legally lack the capacity to make decisions for yourself. You essentially have no legal standing. Should you regain your capacity to make decisions, there is no process for restoring your rights, so it rarely happens. Fortunately, there are several ways to avoid this with proper planning while you still have your full capacity and legal rights.

Establishing and Placing Assets in a Revocable Living Trust

A revocable trust is an entity used to own the property of the grantor (you). The grantor is also the trustee of the revocable trust. Property in the trust is managed by the trustee and is not subject to the probate court system. By designating a successor trustee in the event of your incapacity, you are selecting the person that you want to manage your financial affairs, and not leaving it up to the court to appoint someone.

Creating a Durable Power of Attorney (POA) for Asset Management

A durable power of attorney is a document in which the individual can delegate to an agent the power to make financial transactions on his behalf if he is unable to do so himself. However, the individual must be competent to execute a durable power of attorney, and the agent acting under the durable power of attorney is not subject to regular court review of his or her actions. Assets in one's name that are not titled into the revocable trust would be subject to the POA.

Establish a Health Care Directive or Durable Power of Attorney for Health Care

This document allows you to name a trusted person to make medical decisions for you if you are unable to do so on your own. The person you name is usually called a Health Care Agent. This gives you control over who makes these important decisions for you.

Joint Tenancy

By adding another person to your bank account as a joint tenant, that person will be able to manage the account if you are unable to do so. A revocable trust is far preferable to joint tenancy because a trustee bears a fiduciary duty to act in your best interest. A joint tenant has no such requirement. However, it does allow you to name the person or persons you want to be in control rather than leaving it to the court.

Proper planning is the key to making sure you are taken care of by people you trust. One last word to those who are single adults and have no children—you are more likely to delay establishing your estate plan. You do not have a spouse or children to appoint as your successor trustee or POA, so often these decisions are put off. You may also be delaying establishing your estate plan because you may not be sure where you want your money and property to go. We recommend you talk to an estate planning attorney and get your documents in place. They may just provide the protection you need from being placed under the dreaded conservatorship someday.

Headlines

- FiduciaryPath's Kate McBride and Allan Henriques presented useful insights in *15 Ways to Enhance Donor Trust by Improving Your Investment Stewardship* at an Allodium webinar August 18, 2021.
- The Centre for Fiduciary Excellence (CEFEX) recertified Allodium in August 2021. The annual CEFEX assessment process independently verifies our firm's adherence to fiduciary standards.
- Allodium was listed as one of the Minnesota Registered Investment Advisory (RIA) firms in the RIA Survey and Ranking 2021, as published by Financial Advisor Magazine in the July/August 2021 issue.
- Allodium was pleased to add two new clients during the second quarter of 2021.
- Our office will be closed September 6, November 25 and November 26 for company holidays.

Note: To find out more about Allodium's breaking news, please visit our website: www.allodium.com.

Events

September 15

Dave Bromelkamp will be a moderator for the 2021 Great Plains 7th Annual Institutional Forum on September 15. His panel is called "Practical Steps Towards ESG Integration."

September 30

Are you thinking of purchasing a second home? Or do you already own a second home? Attend our Wealth Management Workshop *Purchasing a Second Home? 19 Things to Know*. We will cover many frequently asked questions and concerns. To register, contact Ilona Avraamides at iavraamides@allodium.com.

WE APPRECIATE YOUR INTRODUCTIONS

To optimize our objectivity and avoid conflicts of interest, we are a fee-only registered investment advisor that is completely independent from banks, brokerage firms and other financial product providers. If you know someone who may be looking for this type of objective investment advice, please contact Dave Bromelkamp at 612-230-3702 or dbromelkamp@allodium.com to arrange a friendly, no-obligation introduction.

Steward is published quarterly by Allodium Investment Consultants. Please contact iavraamides@allodium.com if you have any comments about this publication or wish to be added to or removed from our mailing list.