What is the "Fiduciary Standard" and Why Should You Care?

Welcome to Keen on Retirement
With Bill Keen and Steve Sanduski

Steve Sanduski: Hello everybody. Welcome back to Keen on Retirement. I am your co-host, Steve Sanduski, and this is the podcast where we help you thrive before and during your retirement years. And I'm here with Mr. Bill Keen. And Bill, we have a special guest today.

Bill Keen: I think we should hold our listeners at bay a little bit before we bring this very smart gentleman on. What do you think?

Steve Sanduski: Well, I think you're a tease.

Bill Keen: Yes. In my old age.

Steve Sanduski: That's right. Yeah. Well good. Yeah, well we'll bring on our special guest here in a few moments. I know we've got a listener question that we're going to be going through here today. We have a very detailed question from a listener; lots of good thoughts in there that we'll be riffing on a little bit. But also, Bill, I know you and Matt recently got back from a big conference in Florida. So, why don't we start with you telling us a little bit about the conference?

Bill Keen: For about the last 10 years, we have been invited to an invitation only event for the Barron's Magazine Top Independent Advisors Summit. And we always enjoy that event. It's about a two and a half day event, and we get to attend with other like-minded professionals; mostly fiduciary advisors and firms. But then Steve, also, firms like Schwab, which happens to be custodian. TD Ameritrade, Fidelity, Pershing; talking about what they're seeing happening, the trends in the marketplace, and how they can support us and really support our clients, which is the objective. So, it really helps us to go down there and plug into that think tank of information.

Steve Sanduski: Well, Bill, I know you are a lifelong learner, so you love to continue to learn things, you're curious. So, I am curious, is there anything that you picked up at that conference? Any insight that you thought was pretty valuable?

Bill Keen: It's inspiring to be around what I would consider the best in the world at what they're doing. I think one is we're all focused on bringing total life planning to our clients, and not just talking about the numbers. So many times we sit down with folks who have got issues that go deeper than just, "Hey, what assets do you have in your pension, your 401Ks your ESOPs?" There are family issues, there are things that are happening behind that scenes that if we didn't ask about family tree ... How did you get to the seat that you're in today? Tell me about your life experience. What was it like growing up? What was it like with money? What's your relationship with money? Do both spouses agree on the direction of their lives going forward? And then all the anxiety around a retirement and making that transition. Pretty much across the board, all the firms were in agreement that we need to be having those conversations. Especially as fiduciary advisors and providing perspective to folks.

I'm going to give you one more. We all know that technology is a big deal. It allows us to be even more precise, it allows us to provide a service in result to clients that are definitely better than they were, call it 10, 20 years ago. But the theme at this conference was technology will not replace the human relationship. That clients, we believe, even the millennials, we believe will still be looking for a human-to-human relationship and that technology, while it will help our firms be more efficient, and ultimately the client be more efficient, which is what it's all about, it will never replace the human-to-human relationship. And that was a theme as well.

Steve Sanduski: Yeah, well, and I agree 100 percent with that as well. So, good to hear that. All right. Bill, before ... We're going to keep teasing our special guest here.

Bill Keen: Yes. Are we teaching our listeners or are we teasing him?

Steve Sanduski: We're teasing the listeners, yes.

Bill Keen: Okay.

Steve Sanduski: The special guest knows who he is.

Bill Keen: Yes, okay.

Steve Sanduski: All right. Now, I also want to talk about the F word. Okay? Fiduciary.

Bill Keen: Okay. Yes.

Steve Sanduski: I know we talk about ... We say fiduciary frequently on this podcast. I think, first of all, Bill, if you could give a definition of what a fiduciary is, and then let's just briefly talk about what legislation is happening here as it relates to this idea of being a fiduciary.

Bill Keen: Well, Steve, there's two ways that someone can work with a financial professional. And most investors don't know the difference and wouldn't know the difference unless they were advised about the difference. The first way is called the suitability standard. That's where a broker can make a product recommendation; in most cases receive a commission for the transaction where no real advice was rendered about the transaction or about an overall financial situation.

Now, a much higher standard is called the fiduciary standard. And that's where an advisor has to step in and really look at what's in the client's best interest. This is where we believe that anyone should be receiving financial advice should be working with a fiduciary who's really not just looking at a product sale in a vacuum, but looking at the client's total picture.

Steve Sanduski: Yeah. So, there's been a lot of talk in our industry as you well know, Bill, about trying to require more financial advisors to fall under this higher fiduciary standard. And you and I believe that's a good thing, but there are forces in the industry who are selling products who don't want to be held to that higher standard. So, what just happened here recently with some legislation?

Bill Keen: The annuity industry and the brokerage industry were really putting up a fight. As of just a few weeks ago, they have prevailed in their fifth circuit appeal against the DOL's fiduciary rule. And here was their argument; it's interesting. Now, this is notwithstanding their advertising and the titles on their business cards for their brokers. What they've made the case for, is that their brokers and annuity agents are not advisors at all, but mere salespeople who do not have a relationship of trust and confidence with their clients. That's their argument.

Steve Sanduski: Yeah.

Bill Keen: So, their commission-based compensation is not in any way a payment for the delivery of advice, but merely for affecting a product sale. And that's in their words. So, is there a place for someone to go find a broker and get a product transacted for them? I would say there is. If someone knows they need to go buy a term life insurance policy, and they just want to go find the best price and they approach a broker and they get that bought for them, then maybe that doesn't have to be a fiduciary relationship. I can see where there's places where it doesn't have to be this fiduciary relationship, but for me, it's about how is the broker holding themselves out to the public? What are they saying? What do people think is happening for them on the planning basis? And then what is really happening?

Steve Sanduski: Yeah. I think that's the key point there, Bill, in that you cannot have your cake and eat it, too, when it comes to brokers. So, brokers cannot be legally held to this lower suitability standard while to the consumer public, they're trying to hold themselves out as someone who is giving advice, and they're not just a product salesperson. So, they can't have it both ways, but I agree with you. I think that there is a place for people who sell products. Okay? They're nothing wrong with products. We need products. But the way you've structured your business, Bill, at Keen Wealth Advisors, is you guys are fiduciary advisors, so you're working with people who are looking for a meaningful, trustful relationship that goes beyond just products where people are looking for the lowest price.

Bill Keen: It's my opinion and my experience that for someone to be successful long-term. And for me, being successful is having a financial plan in place so that at some point, someone becomes financially independent. That means they don't have to work anymore if they don't want to. And they're able to make decisions over the course of a lifetime as things come up as life changes that enables them to maximize their resources, minimize their stress, and have that relationship that you mentioned of trust and confidence with an advisor.

And I think that's so important. If someone goes into a firm where they're just being sold a product like a one-off annuity or a stock or a mutual fund or something for a commission, they may think they're getting the depth and level of expertise and ongoing counseling, and they're just simply not.

Anyway, I thought it was good to bring this up. I think this DOL rule, while it might not be the DOL that brings it back; it could be the SEC, it could be some other agency. I think we're going to see it because, again, in some form.

Steve Sanduski: Yeah. It's something, as you know, that's been talked about a lot in our industry for the past few years. So, we'll just have to see what happens over time. But I think that's a good segue into our special guest here, because you were talking about the importance of planning. So, Bill, why don't you introduce our special guest.

Bill Keen: Today, we have on the show, the head of our financial planning division here at Keen Wealth. His name is Rey Arellano. Rey, welcome to the show.

Rey Arellano: Thank you. Thank you, Bill. A long-time listener. Decided to be part of the podcast.

Bill Keen: Rey's a long time listener of the program. Now, you listened to our program before you joined Keen Wealth, didn't you?

Rey Arellano: I did, actually. Probably about four or five months before I joined the team. It was one of the reasons why I wanted to join the team, because it gave me an insight of how the firm thinks when it comes to financial planning.

Bill Keen: Rey has his undergraduate business degree and then he also has his MBA with an emphasis in financial planning. He's also a chartered retirement planning counselor, and he is a certified financial planner as well. One of the other things that I wanted to mention about Rey, too, Steve, is ... I know you saw him when you were in town recording in our studio here; you and Linda. But Rey is a military man. He did six years in the air force. And correct me if I get any of this wrong, Rey, but he did six years in the air force and spent time in Kandahar. Is that right? Afghanistan?

Rey Arellano: Afghanistan, mm-hmm (affirmative).

Bill Keen: And also in Iraq?

Rey Arellano: Mm-hmm (affirmative).

Bill Keen: And also in South Korea.

Rey Arellano: Yes.

Bill Keen: So, and then also some time in Italy as well. Which one do you prefer? You prefer Italy, I would suppose.

Rey Arellano: Yeah a little bit friendlier.

Bill Keen: Little friendlier.

Rey Arellano: The locals really liked us there.

Bill Keen: With some of the things that are happening right now with North Korea ... We chatted with Rey about some of their operations.

Rey Arellano: We always had exercises to be prepared because it only takes about eight minutes to get from North Korea to South Korea. So, our time frame was those eight minutes to make sure everything's in line so we can hunker down.

Bill Keen: Wow, wow.

Rey Arellano: We did that about once a month.

Bill Keen: Wow. Okay. So, coming into Keen Wealth is not quite as exciting, I guess.

Rey Arellano: It is for different reasons.

Bill Keen: Yes, that's right.

You heard us talking about the fiduciary aspect of things.Do you have any examples of things you can think of? Because I think one of the things that's fun about our podcast here is that we go behind the scenes. It's kind of a look behind the curtain. And we don't mind bringing things to the table that are happening in the firm.

Rey Arellano: Yeah, I was really excited to be on this podcast specifically because of the topic of the fiduciary rule. About a month ago, we had a prospect come to us, wanting a second opinion because he worked for a company for 20 years. But before that, he worked for the state of New York for 20 years. He was getting all his paperwork ready to retire and develop a retirement plan, and the advisor he was talking to really wanted to cash in that New York pension plan and put it into annuity, thinking that that was the best outcome for the retirement plan.

Bill Keen: So, let's tell the listeners ... If you have a pension you've earned, some cases, you can take it monthly for the rest of your life, or they'll run a calculation and they'll give you a lump sum. "Here. Here's your money, take it." And it's over. You handle it as best you can. And you're saying this broker was recommending the person cash their pension in, take the lump sum, and put it into an annuity product?

Rey Arellano: Right. Cashing in the pension is not an automatic decision. There's always ins and outs and intricacies in peoples' finances that we need to discuss to see what is the best outcome for the specific person. What kind of struck me was that I don't think that this advisor took the whole holistic picture into account, because the lump sum or the pension is all part of a holistic plan. And what he didn't take into account is that the pension plan in New York has something called a cost of living allowance that grows as you age.

What we did here at Keen is that we took in all his retirement documents, his current 401K, his current pension. The monthly payout or the lump sum, and we just did analysis on what would have the higher probability of success in retirement. And what we came to the conclusion of is that we told him to turn on that pension, have that pension as a stream of income, and have that as a supplement to the 401K, as opposed to trying to take that and investing it into an annuity because that pension grew at a very good rate. I think it was about 3.5 percent annually. To get that guaranteed is very exceptional.

Bill Keen: Oh, sure.

Rey Arellano: Especially at this time.

Bill Keen: We would have been better off, had we recommended that this client roll the assets to us in a lump sum form. Now, we wouldn't have put it into an annuity. But we would have been better off to have recommended him bring that asset to us in a lump sum, right?

Rey Arellano: Absolutely. So, the firm would have made more money, but as a fiduciary advisor, we have to advise clients of the conflicts of interest. And we also, most importantly, have to put the client's interests first. And for this specific client, it was better for him to take the pension ...

Bill Keen: Monthly.

Rey Arellano: .... Monthly, and not do the lump sum, because the probability of his successful retirement was much higher than taking a lump sum and putting it into a product. Even though the product was suitable for him, it wasn't holistic enough for the client.

Bill Keen: That's right. That's a great example, isn't it, Steve?

Steve Sanduski: It is, yeah. And I think it just really points out, as you said there, Rey, the difference between a broker who just follows the suitability standard and a fiduciary advisor, which really does what is in the client's best interest. So, good example.

Rey Arellano: Yeah, thank you. That's one thing that I really appreciate about working here at Keen. I don't ever have the pressures or the constraints of trying to sell a product or trying to make a commission or trying to hit a quota. What people pay us is for our professional advice and recommendations. And there is no conflict of interest of being in product A or product B. We do what we do, specifically for the best of our clients.

Steve Sanduski: I think what it comes down to me, Bill and Rey, is one word, which is integrity. What I like about being a fiduciary advisor is there is integrity there because you are doing what is in the client's best interests, as opposed to what might be in your personal best interest as an advisor to sell something that might get you the biggest commission.

Bill Keen: Yeah, exactly.

Rey Arellano: And I love that word, Steve. That integrity word. That's something that really hits home with me because as we learn about our clients, we learn holistically about everything. We learn about their family tree, we learn about their goals and fears. And something that really touches me, is that these people are real people with real families and real situations and I always think about it whenever they're across the table from me, how would I want my mom to be treated? And that's how I want to treat those clients.

Steve Sanduski: Excellent. Well, Bill, I know we've got a listener question that we want to go through, and this listener has a lot of good points in there. So, why don't we dig into that here for a few minutes?

Bill Keen: I appreciate all of the listeners, so thank you all for your attention and for your feedback. We have a lot of individual investors, we have clients of the firm that listen in to our thinking, and then we also have advisors that listen in. I get a lot of feedback.

Now, I have one that came in after we issued our blog on how inflation can pummel your portfolio if you don't plan for it. That came out a few blog posts ago.

This person did a great job in articulating his slight disagreement with what we said, which we appreciate. We don't just read the ones that agree with us always. Do we, Rey?

It says, "Bill, we usually agree on most everything. Let me share my observations about inflation." And he uses his father and mother as an example. He goes through and makes some really, really valid points on how spending can go down as people age. And we typically run inflation out over the course of someone's lifetime, don't we?

Rey Arellano: Right. We usually use it at three percent, which is higher than the actual historical number of inflation, but we do that intentionally because we don't know the future and would rather be conservative. He mentioned that earlier in retirement, they do spend more money, and then it got slowed down, and then once people got a little bit older, the health care costs creeped up. So, usually that's how we see the practical part of retirement. We call it the go-go phase where you start spending money early in retirement because you're young and you want to travel and you want to spend the money.

Things start slowing down and we call that the slow-go phase. And then at the end of life, we call that the no-go phase, where you really just start creeping up with costs because of health care.

Bill Keen: In our listener's question, he says his parents actually retired in 1984. So, he's got a good data set here to pull from. And he says, "Certainly utility, car, gas, travel, food, and medical expenses paid in '84 compared to 2018 have gone up," but lots of other circumstances where there's spending habits. And his father's still alive today, by the way. Says 100 years old. So, the theme of his note to us was "Inflation isn't quite the boogeyman that is often reported."

He says that his parents lived in their mid-60s in a larger house, they traveled a lot, they ate out a few times a week, and they helped grandkids who were failing. Owned two cars, Mom bought nice clothes regularly, and he says it cost Mom and Dad about 72 thousand dollars a year to live on. Okay? So, take that and then move it out 10 years or so to the mid 70s. Moved to a smaller house, less taxes, less insurance, less utilities. After asking themselves, "Why are we keeping this large house?" Traveled a bit less, noticed they didn't trade their cars as often. Finally now weaned the grandkids off from using them as a primary go to for financial help, and they ate out less. At that point, they still lived on 72 thousand a year.

Now, in the mid-80s ... So go another 10 years. They traveled almost none, had landed on, quote, not me, as financial aid to needy family members, ate out only a few times a month, enjoyed church and family events more now free of charge as the primary source of entertainment, drove their cars about six thousand miles a year, bought clothes almost never, had to add more technology to their lives, which actually added cost, but it now cost them 60 thousand dollars a year to live that life. Interesting, isn't it?

Steve Sanduski: Mm-hmm (affirmative).

Bill Keen: Now, in the mid-90s ... His mother died at 91 and his dad was 96. His expenses halved for eating, car insurance, medical. He sold his truck and now only had one vehicle. His family was now in the no-go years and only traveled as a guest of his kids at no cost. Bought no clothes, got them as gifts as a birthday and Christmas, ate out once a month at a church social, watches TV more, became satisfied with hanging out with friends in his neighborhood daily. It cost Dad 42 thousand a year to live that life.

What do we see, Rey, as a problem with people coming in and saying, "We want to spend more money in the first five years or 10 years of retirement?" Where they hear something like this and it's valid. It's valid. But they say, "Gross our distributions up in the first five to 10 years because we're younger, we're doing more." Where do we see a problem with that? And is there a balance?

Rey Arellano: Well, we actually do take that into account if they tell us that because one thing we do is we know what they spend on an annual basis. The first five or 10 years they want to spend more, they want to go on more vacations, they want to buy newer cars. So we implement that in the plan. We say, "We expect you to spend 15 to 20 thousand dollars more for those first 10 years. And after that, then those expenses fall off because we expect you to slow down." The part of the plan that makes it successful is that every year we review those numbers. We have the discussion of, "What's your expenses like? Are they the same as they were last year? What major changes are there to the plan?"

I think that was a great example of someone that spent more earlier in retirement and then it slowed down. That's a very great example because it went probably down by 25 percent. But we expect that. We expect that and if we plan for it, then it gives us a forecast of what their retirement's going to look like. And if there's any wiggle room with increased expenditures.

Bill Keen: A key thing to get figured out before you retire is the spending, because that's the lever that you can pull to make a plan or break a plan.

Rey Arellano: Absolutely.

Bill Keen: And we can see it now. There have been over 15 thousand meetings over the years. We can see the plans that are kind of on the brink of breaking, can't we?

Rey Arellano: Mm-hmm (affirmative).

Bill Keen: From overspending. We really want people to get clarity on this spending before they retire, so that they don't come up and say, "My goodness. We thought we needed six thousand a month and we really need nine." Or they're almost in denial about it, hoping that it works out. And that's not a great place to be, is it?

Rey Arellano: Right, no. It's never fun to tell someone they need to cut their spending. But through this planning process, I've also had the exact opposite problem, where we have to tell people to spend more money.

Bill Keen: We don't have to tell them that, right?

Rey Arellano: Well, we tell them that they have the ability to spend more money. And it's one of the fun parts about being a planner, is that we know what assets they have and we know what goals they have. And we've actually had to force people to take vacations.

Bill Keen: Well, wait. Let's clarify that.

Rey Arellano: Well, not force.

Bill Keen: Right, right, right.

Rey Arellano: But in our planning, we say, "Hey, we have 12 thousand dollars for vacations, we have it scheduled, we have it locked in there for 10 years. Now, you don't have to go on vacation, but we do have it accounted for. So, if you book those tickets, you have Rey and Bill's blessing some of the advisors want you to save as much as you can and spend as little as you can.

Bill Keen: Right. Because they have more assets to get commissions on.

Rey Arellano: Right.

Bill Keen: Okay.

Rey Arellano: And us fiduciary advisors, we really want you to enjoy the money that you worked your whole life building up. If it includes going on travels, then let's plan for it. If it includes gifting to grandchildren, let's plan for it. But as long as you have a solid plan, we're confident that you'll have a successful retirement throughout the rest of your life.

Bill Keen: "Control the controllable and then have a plan in place to be able to respond appropriately. Not reactively, but appropriately to the things that come up that are unexpected."

Rey Arellano: Exactly.

Bill Keen: And there will be those things. I wanted to say thank you to Steve who submitted this question to us. That's two weeks, two podcasts in a row we've had some really good, detailed questions that came in. And I'll read his final paragraph. He says, "I am sorry this was such a long response to you and I hope you had a few minutes to read it all. My theme was inflation does not impact most retirees as badly as everyone preaches. I believe a financial planner's value can be enhanced by discussing spending habits ..." I agree. "... Life style evolution ..." That came from the Barron's conference I just mentioned, "...And aging." And I agree with you, Steve. "And I have no doubt that you are addressing these to your discussion with retirees! Loyal listener and reader, Steve H."

I really do appreciate it when someone takes the time to submit a question like that. It's fun, isn't it, Steve?

Steve Sanduski: It is, yeah. And it's great, Rey, having you on the show here. I think you've got a future in broadcast journalism. So, really nice job in communicating some of these complex ideas.

Bill Keen: Don't be giving him any ideas. I need him here to at Keen Wealth.

Steve Sanduski: Yeah, that's right, Bill. We don't want Rey to be starting his own gig here.

Bill Keen: That's right. I'll support him in his journey.

Steve Sanduski: That's right. Good. Well, hey, I think that'd be a good place for us to wrap up here. Bill, any final thoughts?

Bill Keen: You know, we always encourage folks whether they're working with us at Keen Wealth, or they're working with another firm, is to go out and continue to stay educated on these topics, to plug into resources like our podcast. We do live events as well; they're educational in nature. Go out and learn the language, listen to what's happening, and really get engaged. We're not trying to make people financial advisors, but we do think it's great that folks get engaged.

So, if we've said something today that resonated with someone or we've given some information that has someone thinking about something they weren't, then I think we've been successful.

So, Steve, thank you for your continued efforts in producing and co-hosting the show with us. And Rey, thank you so much for one, your efforts at Keen Wealth and for your passion and your integrity in how you operate.

Rey Arellano: Thank you.

Bill Keen: I really appreciate having you aboard.

Rey Arellano: It's a pleasure. Thank you.

Steve Sanduski: All right. Well thanks, guys. Great show. And we'll look forward to the next episode of Keen on Retirement.

Bill Keen: All right. Thanks, Steve.

Rey Arellano: Thank you, Steve.