Consider This Program

Episode Date:

February 15th, 2020 Episode

On This Show:

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Show Notes:

Topics Include:

- A Buffered Exchange-Traded Fund (Andrew Thrasher)
- Social Security Timing
- Annuities
- Trustees & Executors

A Buffered Exchange-Traded Fund (Andrew Thrasher)

We have our chartered market technician, part of our allocation team, one of our portfolio managers: Andrew Thrasher on the show today. We've been talking about a new tool that we have added to our box that you've been studying for a little while called a Buffered Exchange Traded Fund. What does that mean?

There's different kinds. There are ones called “buffers” or “defined outcomes.” When you look under the hood, it's an ETF that uses options within the strategy. They provide or attempt to provide some downside protection to the market based on the different option contracts that they're able to use each month. The way different ETF companies operate is each month they create a new fund based off of volatility. They create these buffers. They create these downside levels to where if you were to purchase it on the day it was issued, then it provides protection down to that level. If it was a 10% buffer, then theoretically it's supposed to be able to provide downside protection for the first 10%. If the market were to go down 20%, then you're still exposed to market loss there. They're able to cap the upside. It's a unique product where it's able to provide downside protection for more minor market decline. These are not for everybody. You shouldn't put all of your money inside of them, but it is a tool in the tool box.

How long did you and Adam study backtesting? We put a lot of time into it and then we would actually meet with the people that are behind the scenes that run these funds. Not only the fund companies, but I was able to spend time with the actual fund managers who are buying those options and constructing the portfolios. We really try to understand what's going on before we start putting them into our own models. We continue to have conversations with the back office team behind the funds, just to make sure that as things progress, we understand what's going on within the funds. It's just like what we do with any other investment.

How often would you say we've been able to introduce new technology or a new way into our processes? Is it once or twice a year, as we look at the risk barometer or would you say it's even more than that? We try to screen out as much as we can. We don't really introduce a lot of new ideas. We really want to see things that are battle-tested. How have they done in down markets, in up markets and in stress tests? Once or twice a year, we find something that's considered new that we'd consider putting in our portfolios.

Social Security Timing

What are your timing options? The president mentioned making some changes to Medicare and a little bit on Social Security. It needs to be revamped. Right now under the current law, you can take Social Security as early as age 62. Anybody can apply for it. Under the current code, age 70 is the maximum benefit you can get. If you took it early, would you get more or less? The total lessens because I would need it for a longer amount of time. They would maybe make the payments smaller.

The IRS tells us about 70% of people take Social Security the first minute they can get it. Take into consideration any other income, pensions, IRA money, consideration trust funds, etc. When you take Social Security early, you're going to lose 6% a year of your income. If you take it after your full retirement age, you actually gain 8% a year every year you delay, yet very few Americans really do that because they justify confirmation bias in their own head.

Would it make sense if your health was not good? We have a checklist of 23 things that we use when it's time for you to make a decision. The first one would be health. If you're not going to make it to life expectancy, you probably should take it out. How would your taxes impact your return if you waited longer? If you did have additional funds, then it would make more sense to wait longer, when we're able to employ bracket bumping and deduction stacking and a few other things.

Annuities

An annuity can best be described as a pension. What is a pension? I'm going to take a certain amount of money and I'm going to pay you an income for a certain number of years (usually for your life). Only an insurance company can provide an annuity. They have different cash reserves, different financial requirements than anybody else.

What do you do if you already own an annuity? If you sit down and understand the fees and expenses you're paying and the lack of liquidity, you become frustrated. The people who tend to sell them are not fiduciaries. We don't sell any products.

I'm going to share with you in terms of a variable annuity, because a lot of people have bought those.

One of the new guys on our team was a school teacher for 14 years. He had a 403(b) contract at the school he taught at, which means he had a variable annuity (big carrier, big company). The first thing we made him do was break down an annuity so that he understood what it was. If you're working with a fiduciary, like us at the Financial Enhancement Group, part of our job is to go into your annuity every year, every quarter, however often it is needed, to reallocate those investment funds based on what's going on. However, if I'm a broker, not a fiduciary or a registered investment advisor, I am not allowed to tell you that you should move from large cap to small cap right. I can set up a system to do rebalancing that says, "I want the percentages to stay here and when this one gets too big, please fix it." I can do that, but I can't pick up a phone and call you and say, "you need to move money from here to here."

As fiduciaries, we're not going to call you and say it's time to make a change. We actually go in and do it. When you buy a product from somebody who sells it to you where there is a commission, you have take on that role of responsibility. Our job here at the Financial Enhancement Group is to treat your money as if it were our money and we were in the same situation. That means I'm not going to let money sit there for five years without being examined.

It's something that is an ongoing occurrence that has to happen with someone that sells commissions. They just have to do something that's suitable in that given day, but in any relationship, there is a fiduciary. People fail to understand that for the most part, it's you. It's the person saying yes to buying the product. You're functioning as your own fiduciary. You've got your own responsibility.

We're happy to help you take some of those things that you've done and figure out the best strategies going forward. One of them is a 10% free withdrawal rate on almost all commissionable based products. That doesn't mean you want to ignore the taxes.

Trustees & Executors

One of the last important decisions that you will make, that you can change is: who should be your executor or who should be your trustee if you have a trust? Those are tough questions. What is a trustee? A person who takes care of a trust. What's an executor? If you have a living trust, it's typically the people that are in there.

If you have a trust, you still should have a will, like a pour over will, so anything you forget to put in your trust, you can ask them to put in via the pour over will. The executor, in my case, is the one who takes care of the funeral arrangements and doesn't do a lot of the financial stuff. If you don't have a trust, they have to do the financial stuff too.

1. When you're considering selecting an executor or trustee, should it be a family member, a corporate person, a friend or a combination? How do you decide who it should be?

So if you form a trust, those are typically called a grantor trust. You're making a gift to a trust that you are always the beneficiary of. Temporarily, you are your own trustee. It is very hard to be your own executor because you are not there. You will have to have somebody at some point in time, helping you make financial and life decisions before you die, that person is known as the successor trustee. You and your spouse are typically the trustees. You name other people that are successors.

2. Is it okay to use a family friend?

They need to understand the job requirements and what they've signed up for.

3. With an executor, is that generally multiple people or would that just be one person? Is an executor entitled to be paid?

Most trusts will say that if you are a family member, you don't get paid, but that you can. Many times the trust will kick in because somebody is mentally or physically incapacitated, as opposed to dead. If I'm going to have people make decisions for me which takes time away from building their nest egg, away from their family, I expect them to be compensated.

4. What are the duties made up of?

You assign them in the trust. Most people will say you need to find somebody who is financially aware. That really depends on whether or not you're working with a fiduciary who's helping you manage the money. I always tell people that you want somebody who knows your heart, because they can do a lot. They can change that trust a lot after you're gone.

Disclaimer: Joseph Clark is a Certified Financial Planner™ and the Managing Partner of Financial Enhancement Group, LLC an SEC Registered Investment Advisor. He is the host of "Consider This" found on WIBC Saturday mornings from 6-7a.m. as well as three other Indiana-based radio stations. Joe has served as an Adjunct Assistant Professor at Purdue University where he taught the capstone course for a degree in Financial Counseling and Planning.

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