The Department of Labor (DOL) has given our industry a gift. When the recent DOL guidelines were announced, most advisors and firms shuddered. They envisioned more red tape, Big Brother, and additional confusion. But it turns out the new DOL rules are good for investors and they are good for advisors and their firms, too—at least for those who know how to turn lemons into lemonade.

The lemonade results from leveraging technology to improve investor and advisor outcomes and ensuring DOL compliance by completing the following tasks:

- Record the rationale of and tracking all trade recommendations
- Suggest how to optimally implement these recommendations across multiple accounts and products to enhance outcomes during accumulation and withdrawal, on both an ad hoc basis and systematically
- Quantify the benefit in dollars, basis points, and percentages of optimal implementation during accumulation and withdrawal
- Demonstrate enhanced value to the investor of consolidating more assets with the advisor

In this article, we explain the new DOL requirements, review the key components of goals-based wealth management, and discuss how the combination provides significant benefit to all constituents—investors, advisors, and firms.

**BEST INTEREST CONTRACT**

A Best Interest Contract (BIC) must:
1. Acknowledge advisor is a fiduciary
2. Adhere to “Impartial Conduct Standards,” which require the advisor to:
   - Give advice in client’s best interest
   - Charge no more than reasonable compensation, e.g., scope of services, meeting/advice frequency, advisor expertise and experience
   - Make no misleading statements about transactions, compensation, or conflicts of interest
3. Implement policies and procedures to reasonably prevent violations of Impartial Conduct Standards
4. Firm refrains from incentives for advisors to act contrary to customer’s best interests
5. Fairly disclose fees, compensation, and conflicts of interest

**DOL Requirements**
The new DOL rules are designed to prevent investors from having retirement assets rolled over to higher-fee services that are not in investors’ best interests. To this end, the DOL has listed three types of “prohibited transactions.” They are the following:

1. Rolling from a low-fee 401(k) or individual retirement account (IRA) to an IRA with higher fees
2. Rolling to an IRA where the financial advisor will earn a fee that (s)he wasn’t earning previously
3. Rolling a client from a commission-based account to one with recurring asset-based fees.

These transactions violate the new DOL rules unless the financial advisor can show the rollover complies with a best interest contract (see sidebar for a summary).

Essentially, the DOL requires that an objective, systematic approach must be taken to ensure the following:

- Financial advisors operate from the fiduciary standard of placing the client’s interest first by giving advice in the client’s best interest, being transparent about the fees they charge, and providing services worthy of those fees.
- Firms must have policies and procedures in place to track these operations and ensure that these goals are met from a supervisory and enforcement standpoint by making sure there are no conflicts of interest, disclosing fair compensation/costs, and ensuring value.

**Goals-Based Wealth Management**
Goals-based wealth management (GBWM) describes a holistic process that coordinates the optimal management of all a client’s investment assets across all the client’s
accounts. This includes meeting the client’s risk requirements in a tax-optimal way. It begins with the planning process and goes all the way through to the ongoing execution of the plan over time. The objective is to maximize the capacity of those assets to achieve desired goals. The Money Management Institute (MMI) defines GBWM this way:

The comprehensive management of investor assets—from accumulation through withdrawal and bequest—to help investors achieve optimal outcomes across the multiple accounts and products often found in a household.

Elements of GBWM include: goals-based planning, product and investment selection, asset allocation, and multiple-account optimization.

Multiple-account optimization includes optimal: asset location, rebalancing, and income sourcing and withdrawal sequencing from multiple accounts and products.

The GBWM process begins with the identification and prioritization of investor goals. It includes determining the risk tolerance and appropriate household asset allocation, tax-optimal implementation across each of the multiple accounts and models found in a household and is sustained by regularly monitoring investor milestones against stated goals and making adjustments as circumstances change and providing the optimal sequence of withdrawal across multiple accounts.

By rolling over retirement assets so the advisor can manage a client's taxable and tax-advantaged accounts in a coordinated and tax-optimal way, advisors can deliver better results during accumulation and throughout retirement and can positively impact bequests. And, they can deliver the type of premium service that justifies the rollover under the new DOL rules.

Advisors who use this approach report they enjoy greater wallet share of the client's assets because they are able to quantify the value this process reveals, and so they can make a compelling case about why the investor is better off consolidating assets under one advisor.

**DOL Requirements + Goals-Based Wealth Management = Improved Outcomes, DOL Compliance, and Asset Consolidation**

Figure 1 shows a schematic of goals-based wealth management in action. By aggregating household accounts and completing a goals-based financial plan where the asset allocation and the appropriate product mix and investment strategy are determined at the household level, the advisor coordinates multiple products and accounts both with the initial set-up and on an ongoing basis.

But this can be a difficult and time-consuming process. Advisors report that their clients typically own between five to eight accounts. Advisors also report that they find it challenging to optimally manage all these accounts because of the complexity of daily market movements; the many different products investors have purchased over time; and the different tax treatments that come with these products due to their structures as well as whether they are held in tax-deferred, tax-free, or taxable accounts. Add the consideration of asset location, factor the various constraints of different investment models held by the investor, and ongoing monitoring and rebalancing during the accumulation phase, and this becomes an unwieldy process.

The accumulation phase, however, is relatively easy compared with making intelligent withdrawals, whether on an ad hoc or a systematic basis. Complexity increases as the client seeks to draw income from multiple account types and products and the advisor seeks to maintain the target asset allocation, minimize taxes, and ensure that the investor doesn’t run out of money.

But it can be done, and help is available. By using a combination of software tools available on the market today, an advisor can combine the following:

- financial planning
- account aggregation
- asset allocation
- product selection
- asset location
- model assignment
- monitoring

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<th>GBWM COMPONENTS</th>
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The overall target allocation for the household is Moderate as shown below:

**POTENTIAL BENEFITS**

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<th>Allocation Drift</th>
<th>Annual Return</th>
<th>10-Year Return</th>
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<tr>
<td>+0.97%</td>
<td>+14.87%</td>
<td>4.00%</td>
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**TARGET ALLOCATION**

The overall target allocation for the household is Moderate as shown below:

![Pie chart showing target allocation](chart)

- **Diversified** 4.00%
- **Cash** 3.00%
- **Managed Futures**
- **Government Bonds** 6.00%
- **Corporate Bonds** 6.00%
- **Mortgage Backed Bonds** 16.00%
- **TIPS** 4.00%
- **High Yield Bonds** 7.00%
- **Emerging Markets Bonds** 2.00%
- **Emerging Markets Equity** 3.00%
- **International Equity** 13.50%
- **Mid Cap Equity** 2.50%
- **Small Cap Equity** 1.50%
- **Large Cap Equity** 27.50%

**Estimated benefit over 10 years**: $148,729

Compared to management using a typical pro rata approach (where each account is managed individually against the same target), taxes can be streamlined by assigning the components of the household target to the accounts in which they will be the most tax-efficient.

- **4.50% Allocation Drift**
- **+0.97% Annual Return**
- **+14.87% 10-Year Return**

A GBWM approach may entail more complexities, but with it come significant opportunities that also are made efficient by automating certain functions. Software exists that quantifies future benefits and shows how to tax-efficiently coordinate the management of multiple account registration types, including trade instructions for how to optimally manage these multiple accounts and products.

Managing these elements in a tax-efficient and coordinated way can add 100–200 basis points per year in incremental after-tax returns, according to Blanchett and Kaplan (2013) and validated in an independent analysis by Ernst & Young. Figure 2 shows that, for a typical client with $1 million in investable assets, this can translate into as much as an additional $148,729 to be kept by the client and not paid out in taxes.

The objective of the DOL fiduciary standard is to ensure that clients are getting the most out of their assets during accumulation as well as in retirement. Doing “all of the above” goes beyond the current practices of most advisors, but “all of the above” can provide enough additional incremental after-tax return to justify rollovers. And for good reason. Boston Research Group (2009) found that it takes one to three hours per client account to determine the most tax-efficient withdrawal for one withdrawal. That’s obviously time-consuming and just not scalable for advisors. But existing software makes it possible.

By managing a client household in an optimal and coordinated way, the advisor and the firm meet the DOL definition of the fiduciary standard of acting in the client’s best interest by doing the following:

- Rebalancing
- Optimal withdrawals

**GBWM Components**

The following includes brief descriptions of each of the components of GBWM:

**Financial plan:** Goals-based wealth management starts with a plan based on the goals the client has determined. Financial planning tools abound and will become more important to demonstrate that the advisor understands the client’s objectives and is in a position to add value.

**Account aggregation:** To provide comprehensive advice, it’s always best to see all of a client’s assets so the advisor has a complete picture and can recommend how best to advise the client in meeting goals.

**Asset allocation:** To help a client navigate the ups and downs of the market, it’s...
vital for the client and advisor to agree to an appropriate target asset allocation and also to review that decision over time so the client can be educated about risk and potential consequences as markets change.

**Product selection**: Most clients have purchased products over time and it’s important to review whether those purchases continue to meet client objectives. Considerations increasingly have and will continue to be about cost and how the products work in combination.

**Asset location**: Planning tools typically make asset allocation recommendations at the household level but do not recommend where the assets should be located between taxable, tax-deferred, and tax-free accounts. Blanchett and Kaplan (2013) points out that 50 basis points per year in incremental after-tax returns can be achieved by locating assets in the optimal and appropriate accounts. Software exists to help advisors optimally locate assets in the various accounts of a household. It also quantifies the value of the improved outcomes. As markets and circumstances change, it is vital to optimally manage asset location on an ongoing basis.

**Model assignment**: Buying managed accounts, or models, for a client is an effective way to achieve a desired risk profile or asset allocation. However, significant tax benefits can be achieved by assigning particular models with certain characteristics to one type of account—taxable or tax-advantaged—and some models to another type. This is related to asset location, described above.

**Monitoring**: Goals-based wealth management coordinates various accounts and product types within a household and so must the monitoring of those accounts and product types. It is not enough to monitor a portfolio on a single account level; it must be done at the household level. For example, how does the increase in a client’s technology holdings in one account affect the desired risk target of the entire household portfolio?

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**DOL-ADVISOR CASE STUDY: 1 + 1 = 3**

The following is a case study that shows how a financial advisor who uses coordinated multi-account optimization software responded to a client about meeting the DOL fiduciary standard:

**Client description**: Married couple in their mid-50s with three children; husband given an “early retirement opportunity.” The couple own six accounts—two-taxable, two IRAs, and two 401(k) accounts—spread among three advisors with this advisor managing half the assets. Assets total $1 million in household investable assets.

**Client question**: I’ve been reading about the DOL fiduciary standard. What does it mean to me?

**Advisor response**: The DOL fiduciary standard says I need to keep your best interests in mind and charge no more than a reasonable fee when I make a recommendation on a rollover from an IRA or a 401(k) account. This is what we’ve been discussing as you leave your company.

Our firm has incorporated sophisticated software into my workstation that helps me provide you with an enhanced level of advice and allows me to find ways to improve your outcomes. Our system offers guidance on the optimal way to manage your taxable and tax-advantaged accounts in a coordinated and tax-efficient way to improve your after-tax returns and income. Through this process of minimizing taxes across all your accounts and products, we will keep your risk in line with what you’re comfortable with and track goal achievement over time.

The DOL says I need to provide advice on an ongoing basis. Our system helps me continuously monitor client accounts and automatically alerts me when action is needed to further minimize taxes or to get closer to the risk level you’re comfortable with.

Our system also keeps track of the recommendations, such as for tax purposes or to more closely track the target allocation, which allows me to be fully transparent about all investment transactions. This is something the DOL also wants me and my firm to keep track of.

My firm has its own set of DOL rules to follow. The DOL requires the firm implement policies and procedures designed to prevent advisors from violating what are called the Impartial Conduct Rules. Once again, our system helps ensure this by: (1) enabling the firm to monitor advisors’ activities by keeping an audit trail of why each buy or sell was suggested; (2) automating an alert process to notify me and other advisors when a client’s portfolio needs attention; and (3) recommending specific financial products or models that are appropriate for each client.

**Result**: The couple consolidated assets with the advisor after they were shown the tool that quantifies the benefit of tax-smart optimization and saw they would realize an extra $127,435 in improved after-tax returns and income over the next 10 years. The advisor went from managing $450,000 of client assets to managing more than $1 million in client assets, improving his fee-based compensation by $5,500 in the first year. The firm netted two birds with one stone by meeting the DOL fiduciary standard at both the advisor and firm level and improved the client’s outcome as well as the advisor’s and the firm’s results.

**Rebalancing**: It is not sufficient to rebalance individual accounts within a portfolio without considering the entire household. When positions are increased or decreased within individual accounts, such changes must be made with consideration of how they affect the overall target allocation across all accounts held by that household.

**Optimal withdrawals**: The 4-percent rule of thumb for withdrawals is as outdated as what advisors were once called—“customer’s men.” The typical household owns multiple accounts and account types, markets change daily, and life’s circumstances transform over time, so the optimal withdrawal methodology considers taxes and targets risk to determine the capacity of assets in retirement. Software exists that can recommend the optimal sequence of withdrawal from different account types and maintain target asset allocation and optimize asset location. According to Blanchett and Kaplan (2013), optimal withdrawals can improve after-tax
returns and income by 54 basis points per year. This software suggests the optimal sequence of withdrawal and quantifies the benefit of the optimal income distribution.

**Summary**

Lemonade anyone? By combining a comprehensive GBWM approach utilizing readily available financial technology tools, financial advisors are now in a position to improve investor outcomes—as well as their own—as they ensure DOL compliance. They can do this by:

- Understanding the client’s objectives for household investment assets and suggesting optimal management across multiple accounts and products to enhance investor outcomes during accumulation and withdrawal, on both an ad hoc basis and systematically.
- In doing so, electronically record the rationale of all trade recommendations.
- Quantify the benefit to the client, in dollars and cents, of the optimal implementation during accumulation and withdrawal. This will demonstrate the value the advisor brings above and beyond product selection.
- Clearly presenting to the investor the enhanced value of consolidating more assets with the advisor.

By combining a comprehensive GBWM approach utilizing readily available financial technology tools, financial advisors are now in a position to improve investor outcomes ... as they ensure DOL compliance.

Jack Sharry is executive vice president of strategic development for LifeYield LLC, a developer of software to help financial advisors and investors achieve optimal after-tax returns and income through coordinated, multi-account management. He is also chair of the Money Management Institute’s (MMI) Digitally Enabled Advice Committee. Contact him at jack.sharry@lifeyield.com.

**Endnote**


**References**


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