The Value of Financial Advisors to Retirees

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Abstract: *This study explores the value of financial advisors to retirees, in terms of both the likelihood of the retiree to undertake planning activities and his/her feelings of confidence and financial security. Results indicate retirees with financial advisors are more confident their assets will cover retirement expenses, more confident their assets are being managed in the best way possible, and feel more financially secure. Additionally, retirees with financial advisors were more likely to undertake all planning activities compared to those without an advisor, and were more likely to have thought about certain important issues.*

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Introduction

Current and future retirees face circumstances that in previous generations were not as apparent. These circumstances include the decreasing availability of traditional defined-benefit pension plans, increasing longevity, and rising health care costs. Current and future retirees will be faced with the difficulty of planning for these circumstances, which relies on new research, strategies, and techniques to face this new norm of living longer on managed assets. Due to these factors, it is becoming more difficult to rely on the planning experience of previous generations, e.g., the parents of current and future retirees in this new norm.

Research has examined the characteristics of those who choose to hire a financial planner or seek financial advice.[1] However, research relating to the value of hiring an advisor is sparse. This study explores the differences in terms of confidence, feelings of financial security, and planning activities undertaken by retirees with a current financial advisor.

Setting the Stage

Both planning behavior and characteristics for retirees without traditional defined-benefit pension plans were analyzed based on the retiree's use of a financial advisor. Previous research has determined factors associated with using a financial advisor; however, we are only beginning to examine the differences in those who do and do not work with financial advisors.

The FPA and Ameriprise Value of Financial Planning Study[2] provides insight into the client-planner relationship and the benefits of using a financial advisor. Differences were apparent between those who received either advice only or comprehensive planning, compared to those who planned for themselves. Notable differences included higher confidence, greater feelings of financial security, and a greater likelihood to have undertaken planning activities such as having a plan for retirement income and estimating retirement income needs.

Through other previous research, we also know a lack of planning behavior exists. *The Retirement Confidence Survey*[3] (RCS) suggests that only half of those saving for retirement calculate an adequate savings amount; rather, many individuals simply guess this amount. Many workers plan to work longer; however, the same survey suggests this does not always occur. The primary reason cited for early retirement was health issues. The RCS also found that in 2008, 29% of respondents were confident they had saved enough assets to live comfortably, while 35% reported being somewhat confident. Nearly half of retirees were not confident in paying for medical expenses during retirement as the current estimate of out-of-pocket health care cost had risen to an at-retirement need of nearly $250,000.[4] Along these same lines, in 2008 nearly half of retirees were not confident in the ability to pay for long-term care expenses. Although these statistics are sobering, they are based on a nationally representative sample including all income, age, and asset ranges. Of note, the RCS did not report differences in using an advisor; however, this survey does provide a glimpse into retiree confidence and planning activity.

Based on this previous research, we hypothesize that retirees without a current financial advisor are not as likely to address important planning activities and are likely to feel less confident and financially secure compared to those retirees with a financial advisor.

Sample of Retirees

This study analyzed a specific area of the retiree market. The study sample of retirees was derived from a survey administered jointly by the Society of Actuaries (SOA), LIMRA, and the International Foundation for Retirement Education (InFRE). Data was collected in February 2008, with a focus on obtaining an in-depth view into retirees' financial decision-making process. Survey participants were chosen based on specific characteristics, including individuals who have been retired longer than one year, between the ages of 55 and 75, and who have $100,000 or more in investable assets. Those who did not meet these criteria were removed from the sample. The sample was further filtered to exclude those who reported having an employee-sponsored defined-benefit plan. The sample was limited to only those who had managed assets that may be needed to produce future income, in an attempt to replicate the new normal of living longer on managed assets. This does not suggest that those with defined-benefit pension plans will not derive income from managed assets, but rather it shows the retirees with these plans have the luxury of supplemental fixed income over Social Security. Further demographic details are located in Appendix A.

Although the sample is not generalizable to the total population of retired Americans, the characteristics of the remaining sample provide valuable insight, not only into planning for this new normal, but into the benefits and value of the client-advisor relationship.

Research Methodology

Retirees with a current financial advisor were compared to those without a current financial advisor by using questions related to confidence, financial security, risk tolerance, and various planning activities and behaviors. Chi-square statistics were utilized to test the differences between the two groups at a $p<.05$ level of significance.

Confidence and Security in Retirement

The retirees were asked two questions regarding confidence in retirement. Confidence in sufficient savings was explored using the question, "How confident are you that you saved enough money to live comfortably throughout your retirement years?" Most retirees were confident that they had saved enough money to live comfortably during retirement, with or without an advisor. The most significant differences appear in the lower levels of savings confidence; 22% of the retirees without an advisor reported feeling "not too" or "not at all" confident they had saved enough while only 14% of those with an advisor reported the lower levels of confidence. These findings are somewhat subjective in nature because the retirees would need to accurately know how much they needed to live comfortably in retirement; however, the sense of confidence was evident (Table 1).

A different dynamic of confidence was also measured, specifically concerning confidence in investment management, which was explored with the question, "How confident are you that your assets and investments are being managed in the best possible way?" Differences in confidence levels were even more apparent between those with and without an advisor. Of retirees without an advisor, only 37% were very confident that their assets and investments were being managed in the best way, while 61% of those with an advisor were very confident. A large variation also existed for retirees rating this question in the lower levels of confidence. Specifically, retirees without an advisor and those with a current advisor, 12% and 3% respectively, reported feeling "not too" or "not at all" confident in the way their assets and investments were being managed in the best way possible.

Perception of financial security was also explored in order to determine how retirees' perception compared from preretirement to postretirement (Table 2). Participants were asked, "Are you as financially secure now as you thought you would be when you first retired?" Similar to the confidence questions, financial security was also higher among retirees who currently worked with an advisor. More than half of the retirees sampled, both with or without an advisor, reported feeling as financially secure today as when they first retired. Retirees with a current advisor were more likely to respond they are as or more financially secure compared to when they first retired. The opposite relationship existed for those without an advisor, who were more likely to feel less financially secure compared to when they first retired.

TABLE 1

Confidence

How confident are you that you saved enough money to live comfortably throughout your retirement years?

	No Current Advisor	Current Advisor
Very confident	33.2	31.9
Somewhat confident	44.8	54.5
Not too confident	15.3	11.3
Not at all confident	6.7	2.2

How confident are you that your assets and investments are being managed in the best possible way?

	No Current Advisor	Current Advisor
Very confident	37.3	60.5
Somewhat confident	51.0	36.3
Not too confident	10.3	2.9
Not at all confident	1.4	0.2

Percentage of respondents. Chi-square statistically significant differences exist between each advisor category compared to "no advisor" at the .05 level.

TABLE 2

Perception of Financial Security

Are you as financially secure now as you thought you would be when you first retired?

	No Current Advisor	Current Advisor	Same Advisor Before Retirement
Yes	52.0	56.6	62.7
No, more	17.6	22.4	19.9
No, less	30.5	21.0	17.4

Percentage of respondents. Chi-square statistically significant differences exist between each advisor category compared to "no advisor" at the .05 level.

Planning Behavior

Preretirement Planning Behavior

Planning behaviors—both thoughts and actions—were explored among participants through a series of questions. Though we look at the impact of financial advisors, we do not know the scope of engagement defined between the retiree and the advisor. Hence, it should not be inferred that some advisors may not be doing their jobs since the scope of engagement may have not included certain planning activities. Even in light of this fact, we see that retirees with advisors were more likely to undertake planning activities.

The first set of questions served to examine preretirement planning activities that retirees engaged in to determine if they had the financial ability to retire. Participants were asked, "Before you retired, which of the following activities did you (and/or your spouse/partner) do to see if you could afford to retire?" Those who had their current advisor before retirement were more likely to have planned across every area tested as compared to those without a current advisor (Table 3).

These differences were significant in every case except in determining options to reduce living expenses. Some planning areas still seem deficient, even for those who worked with a preretirement advisor. Only 45% of the retirees with an advisor and 26% without an advisor had identified their retirement income resources for early, mid, and late phases of retirement. The planning activity most likely to be undertaken by retirees was determining whether their income would cover expenses in retirement. Despite being the most likely undertaken, only 69% of these retirees with an advisor and 54% without an advisor had performed this type of analysis. One of the most significant differences between the two groups emerged from the question of estimating how inflation might affect expenses after 15 or more years into retirement. Of the retirees with a preretirement advisor, 44% estimated the impact of inflation while only 26% without an advisor made the same estimate. Health care preparation was explored by asking participants if they had taken into account the fact that eligibility for Medicare benefits begins at age 65. Results indicate that 54% of retirees with a preretirement advisor and 45% without an advisor responded positively to this question.

Timing of Social Security benefits appeared to be a concern for most retirees regardless of advisor affiliation. However, results revealed a 13% difference between retirees who worked with an advisor before they retired and those who did not. The remaining questions appeared to be grossly overlooked by retirees prior to retirement. For example, 28% of retirees with an advisor prior to retirement and 21% without an advisor estimated whether or not they would have to work for pay during retirement. The area most overlooked by the retirees, but possibly not as necessary or desired, was options for moving to reduce their cost of living. Only 22% of retirees with an advisor before retirement and 19% without had considered any options for moving during retirement. Lastly, and most interestingly, was a group of participants who reported having not engaged in any of the above planning activities. Of retirees who reported not working with an advisor, 26% reported not participating in any of these planning activities. Although significantly lower (but possibly too high), 11% of retirees with an advisor prior to retirement reported not addressing any of these areas.

Postretirement Planning Behavior

Planning is equally important after retirement as before. Participants were asked a number of planning questions regarding their postretirement planning activities. Two questions were used to examine specific planning behaviors. Retirees were asked, "Since you retired, have you established specific plans for…?" (Table 4). The first question explored retirees' plans for withdrawing retirement funds during retirement. Results reveal statistically significant differences in planning for withdrawal of funds among retirees without an advisor (44%) compared to those with an advisor (53%). The

TABLE 3

Preretirement Planning Activities

	No Current Advisor	Current Advisor	Same Advisor Before Retirement
A. Identify retirement income resources for early, mid and late phases of retirement			
Yes	26.5	38.3	44.8
B. Determine whether your income would cover your expenses in retirement			
Yes	54.1	61.4	69.2
C. Estimate how inflation might affect expenses after 15 or more years in retirement			
Yes	26.1	35.4	44.0
D. Take into account that eligibility for Medicare health care benefits begins at age 65			
Yes	45.2	49.2	54.3
E. Determine whether you would have to work for pay in retirement			
Yes	21.4	26.9	28.3
F. Compared options for moving to reduce cost of living expenses			
Yes	19.3	23.8	22.3
G. Evaluate when the best time to take Social Security benefits would be			
Yes	53.2	60.1	66.2
H. None of the above			
Yes	26.6	16.5	11.2

Percentage of respondents. Chi-square statistically significant differences exist between each group at the .05 level.

TABLE 4

Distribution Considerations

	No Current Advisor	Current Advisor	Same Advisor Before Retirement
A. Withdrawing funds you saved on your own, such as personal savings, CDs, IRAs, etc.			
Yes	43.8	38.3	53.5
B. Minimizing taxes by ordering the withdrawal of funds from your IRAs and/or Roth IRAs, employer retirement plans, and personal savings, etc.			
Yes	44.7	61.4	59.4

Percentage of respondents. Chi-square statistically significant differences exist between each advisor category compared to no advisor at the .05 level.

TABLE 5

Written Financial Plan

Currently, do you have a formal written plan for managing your income, assets, and expenses during retirement?

	No Current Advisor	Current Advisor
Yes, created before I retired	10.7	28.8
Yes, created after I retired	11.6	23.5
No, but plan to create one	11.5	10.3
No and don't plan to	66.3	37.4

Percentage of respondents. Chi-square statistically significant differences exist between each advisor category compared to no advisor at the .05 level.

TABLE 6

Informal Financial Plan

Currently, do you have an informal written plan for managing your income, assets, and expenses during retirement?

N = 285	No Current Advisor	Current Advisor
No	38.4	21.9
Yes	61.6	78.1

Percentage of respondents. Chi-square statistically significant differences exist between each advisor category compared to no advisor at the .05 level.

second question addressed retirees' planning for minimizing taxes through ordering the withdrawal of retirement funds. Again, results show that a greater percentage of retirees currently with an advisor (59%) had established plans for minimizing taxes compared to those without an advisor (45%).

A second and more general group of questions was asked to determine whether these retirees had a formal written plan for retirement (Table 5). Participants were first asked, "Currently, do you have a formal written plan for managing your income, assets, and expenses during retirement?" The majority of retirees without an advisor (66%) reported not having a formal plan or having no plan to create one. Of those without an advisor, only 22% reported having created a formal plan before or after they retired and 11% reported planning to create one.

Interestingly, a significant portion (37%) of retirees with a current advisor reported not having a formal plan or having no plan to create one. However, over half with a current advisor reported having created a formal plan either before or after retirement. If early planning was the goal, then individuals with the same advisor they had prior to retirement were in the best position for retirement in terms of planning (not shown in table). Over 45% of retirees with an advisor prior to retirement created a formal plan before they retired for managing their income, assets, and expenses and an additional 11% had created a plan after they retired.

If participants reported not having a formal plan to manage income, assets, and expenses during retirement, they were then asked if they had an informal plan (Table 6). The majority of these retirees reported at least having an informal plan. Results reveal statistically significant differences in informal planning between retirees without an advisor (62%) and those currently with an advisor (78%).

Other Retiree Behaviors

Several other factors during retirement can significantly impact retirees' maintenance of their current standard of living. These include, but are not limited to retiring earlier than planned, age at retirement, risk tolerance and subsequent portfolio allocation to equities, and unexpected health care expenses. According to the RCS of 2008, 51% of retired respondents reported retiring earlier than planned primarily due to health, downsizing, or family care. Only 7% offered positive reasons for retiring early.

A large portion of the retirees from the survey indicated they retired earlier than they thought they would. At first glance, it would appear that there is a negative relationship between having an advisor and early retirement. Of retires currently working with an advisor, 61% reported retiring earlier than they thought, while almost 63% of those not working with an advisor reported retiring earlier than they expected (Table 7).

Based on these findings, it appears that individuals with an advisor may be less likely, or as likely, to retire early as compared to those without a current advisor. The important question is whether or not early retirement was financially warranted. To further understand the justification for early retirement we tested two metrics: confidence in savings and an estimate of asset longevity. Looking at those who reported retiring earlier than they expected, slight differences start to appear in savings confidence. Of retirees who currently have no advisor and retired earlier than they expected, 31% were very confident and 47% were somewhat confident they had saved enough money to retire comfortably. Of retirees who had an advisor during the time of the investigation and retired earlier than they thought they would, 23% were very confident and 58% were somewhat confident they had saved enough money to retire comfortably (Table 8).

There is a significant portion of the sample (63% without an advisor and 61% with an advisor) who retired early and the large majority of these earlier retirees were very confident or somewhat confident that they had saved enough money to live comfortably in retirement (78% without an advisor and 81% with an advisor). But was this conclusion reached through an analytical calculation? If choosing to retire at a certain point, it would make sense to estimate how long assets will last during retirement. Some participants may have simply taken a guess at this, as many do when determining amounts to save, while others may have sought the advice of a financial professional, and still others may not have even thought about this at the time they retired. To explore if retirees had thought about asset longevity they were asked, "Have you estimated how many years your assets and investments might last in retirement?" The response

TABLE 7

Retirement Age

Did you retire when you thought you would?

	No Current Advisor	Current Advisor	Same Advisor Before Retirement
Yes	33.1	31.9	39.9
No, earlier	62.5	60.7	51.6
No, later	4.5	7.5	8.5

Percentage of respondents. No significant difference existed between advisor compared to no advisor at the .05 level.

TABLE 8

Early Retirement and Confidence

How confident are you that you saved enough money to live comfortably throughout your retirement years?

	No Current Advisor	Current Advisor
Very confident	31.1	22.6
Somewhat confident	47.1	58.2
Not too confident	14.0	14.7
Not at all confident	7.9	4.6

Percentage of respondents. Chi-square statistically significant differences exist between each advisor category compared to no advisor at the .05 level.

TABLE 9

Estimate of Asset Longevity for Those Who Retired Early

Have you estimated how many years your assets and investments might last in retirement?

	No Current Advisor	Current Advisor
No	38.8	38.7
Yes	43.0	55.3
Never thought about it	18.2	6.0

Percentage of respondents. Chi-square statistically significant differences exist between each advisor category compared to no advisor at the .05 level.

options were "yes," "no," and "never thought about it" (Table 9). Looking solely at those who reported retiring early, 43% without advisor and 55% with an advisor had estimated how many years their assets and investments would last during retirement. The more important results were revealed in the inverse; those who retired early but had not estimated asset longevity. Specifically, 57% of retirees without advisor and 45% with an advisor had not estimated how many years their assets and investments would last during retirement. Even more concerning: almost one in five of these retirees without an advisor had never thought about asset longevity, yet retired early.

TABLE 10

Willingness to Accept Investment Risk

How much risk are you willing to accept when it comes to your assets and investments?

	No Current Advisor	Current Advisor
Absolute minimum	34.4	20.7
Some risk is acceptable	49.4	57.3
Moderate amount is acceptable	14.7	20.3
Reasonably high risk	1.5	1.7

Percentage of retirees. Chi-square statistically significant differences exist between each advisor category compared to no advisor at the .05 level.

TABLE 11

Paying for Long-Term Care Expenses

If you were to need long-term care, how would you pay for this expense?

	No Current Advisor	Current Advisor
Haven't thought about it	25.1	15.6

Percentage of retirees. Chi-square statistically significant differences exist between each advisor category compared to no advisor at the .05 level.

TABLE 12

Purchased Long-Term Care Policy

Have purchased a long-term care policy

	No Current Advisor	Current Advisor
Yes	13.7	28.9

Chi-square statistically significant differences exist between each advisor category compared to no advisor at the .05 level.

Risk tolerance and, ultimately, asset allocation can have a significant effect on asset longevity during retirement as we have seen in recent sustainable-withdrawal-rate research that has shown the need for allocations to equity in order to combat the risks of inflation and longevity over the retirement time horizon. Considering this, participants were asked, "How much risk are you willing to accept when it comes to your assets and investments?" (Table 10). These responses were segmented around the advisor relationship. It is not possible to know the direction of the relationship between risk tolerance and use of an advisor with the cross-sectional data used for the current study. However; it is apparent that there are differences between the retirees who had an advisor, either before or after retirement, and those who did not. Specifically, less than 2% of retirees across all advisor relationships reported high levels of risk within their assets and investments. Across the advisor relationships, the largest dispersions appeared for those who wanted absolute minimum and moderate amounts of risk. More retirees without an advisor (34%) as compared to those with a current advisor (21%) wanted to maintain their asset and investment risk at an absolute minimum. This relationship changes when moving to the "some risk is acceptable" category. More retirees with an advisor (57%) are willing to take some risk compared to those without a current advisor (49%). Similarly, more retirees with an advisor (20%) are willing to take moderate risk compared to those without (15%). Little difference existed between advisor use and taking high risk, and few retirees responded they were willing to take such risk.

Finally, long-term care and unexpected health care costs can be a significant drain on the retirement budget and assets of most retirees and should be planned for accordingly. Participants were asked, "If you were to need long-term care, how would you pay for this expense?" A quarter of the retirees without an advisor indicated they had not thought about how to handle the expenses of long-term care, significantly more than those with a current advisor (16%; Table 11).

Households can use a number of different resources to cover the expenses of long-term care; however, the most secure method would be a long-term care policy. Results indicate that 13% of participants without an advisor, compared to 29% with an advisor, reported having purchased a long-term care policy (Table 12). Note that due to the asset demographics of these retirees, some may have chosen to self-insure against long-term care risk rather than purchase an insurance policy.

Conclusions

Though causality is not suggested of the advisor-retired client outcomes, this study indicates that individuals who utilize the services of financial advisors are more confident, feel more financially secure, cover a greater range of important financial planning activities, and may be in a better overall financial situation than those who do not utilize the services of financial advisors.

Though not all retired clients may have requested comprehensive services of their advisors, some areas seemingly should be discussed across the board. While the exact type of advisor (financial planner, broker, insurance agent, CPA, etc.) was not discussed in detail, the majority of retirees with an advisor (63%) reported working with a financial planner when presented with these options. Considering this, there are certain areas where advisors may be able to add value to their retired client relationships, many of which may require only a simple discussion to bring the area to the client's attention, such as meeting long-term care expenses. Even for advisors working with preretired clients, value can be added through discussion of income sources during retirement, impact of inflation, and the possibility of working during retirement, in addition to the other planning activities.

Based on this study, it is apparent that individuals without an advisor may not consistently perform many of the planning activities discussed in this paper. This is unfortunate in terms of the challenges new retirees will face in the future. Efforts should be made to increase the knowledge of these retirees, and particularly preretirees, as both groups have been suggested to have the same issues in terms of planning for retirement. It is possible that those not seeking financial advice are simply not aware of the important factors relating to retirement planning.

This research suggests individuals with an advisor appear to be more confident that their assets will last, more confident that their assets are well-managed, and have a greater sense of financial security during retirement. Similarly, individuals with an advisor are more likely to have thought about and undertaken preretirement and postretirement planning activities. The question remains whether advisors breed confidence in retirees, or if the retirees are more confident and choose to have an advisor. Regardless, this research indicates a determinable difference in these areas in favor of financial advisors.

This study also empirically confirms what many advisors have long presumed: that retirees utilizing the services of financial advisors may be better situated for financial success. Advisors can use these findings in discussion with clients and potential clients to show the value of the services provided and the psychological implications of increased feelings of confidence and financial security. In addition, we see areas where advisors may not be helping depending upon the scope of engagement; however, there are areas that retirees are not addressing, which represents an opportunity to expand the scope of engagement.

Future Research

Future research in this area is abundant. One area of this particular topic to explore further is the role of an advisor based on scopes of engagement. In this study, "financial advisor" was defined by a broad array of financial services professionals who may not provide a holistic service engagement with the retiree. Also, whereas this study related to the value of advisors to retirees, similar work can focus on the value of financial advisors for preretirees. ■

Editor's Note: Several timely issues are touched upon but not dealt with in this article: the fiduciary standard of care; the comprehensiveness of an advisor engagement; the need for comprehensive financial planning versus specific, narrowly focused advice; and the potential for significant leaps in longevity within the life expectancy of those at or near retirement today.

This article is the starting point of what we hope will be a rich discussion in the coming years on these and related *topics. The editorial staff of this Journal looks forward to continuing this dialogue in future issues.*

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APPENDIX A

Respondent Demographic Information

Variable	**Frequency (%)**
N	1524
Gender	
Male	55.0
Female	45.0
Education	
< High School	0.4
High School	14.1
Some College	30.5
College Graduate	28.4
Graduate School	26.6
Marital Status	
Married	72.6
Widowed	8.6
Divorced	11.6
Separated	0.8
Never Married/Single	6.4
Current Annual Income (in thousands)	
<$15	1.9
$15 to $24.9	9.0
$25 to $34.9	11.8
$35 to $49.9	18.7
$50 to $74.9	24.2
$75 to $99.9	14.9
$100 to $149.9	11.1
$150 to $249.9	5.5
> $250	3.0
Current Debt Outstanding (in thousands)	
Zero	33.5
<$5	16.9
$5 to $9.9	5.6
$10 to $19.9	7.1
$20 to $49.9	10.1
$50 to $99.9	11.4
$100 to $249.9	10.6
> $250	4.8
Investable Assets	
$100,000 to $249,000	30.5
$250,000 to $499,000	27.4
$500,000 to $999,000	24.2
$1 million to $1.99 million	12.5
> $2 million	5.3