It's (Not) All about the Details

by Bob Rall, CFP®

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The retirement projection that I worked hard to prepare and review with one of my clients last week is wrong. In fact, all of the projections I have given to clients over the many years that I have been offering planning services are wrong. And the plans that you've been putting together for your clients are all wrong as well. But before you take offense and get defensive, I'm betting that you already know they are wrong.

Why are they wrong? Because every retirement plan that we put together for a client is built on a number of assumptions. We have to assume a lot of things to put a plan together. We have to make assumptions about when a client is going to retire; what they will spend once they get there; how that spending will change over time; investment returns before and after they retire; inflation rates; tax rates; economic conditions; and many other factors. And of course, we have to try to do the impossible by making an assumption on when our client's plan will end (the nice way that planning software says that the client has passed away).

The Nature of Assumptions

Very few, if any, of the assumptions that we build into the plan will actually be spot on. In fact, even the goals that we build into the plan will change. Not long ago, I did a retirement projection for a client who wanted to include a travel goal of $10,000 per year so she could take her daughters on a nice European vacation every year. So we built it into the plan. They went to Europe later that year. They had a great time and I even got to see some of the pictures. The next year, as we were reviewing the plan, I asked about the travel plans for the upcoming year. She let me know that they weren't going on a European vacation; they decided to remodel their kitchen instead.

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That's why all of our retirement projections are wrong. It's also why I rarely provide clients with the actual projections. I don't want to give them a false sense of security if the projection looks good. And I don't want to make them think their future is hopeless if their plan needs some work. I try to use the plan simply as a guideline. I try to help them understand that, based upon where they are today, they appear to be on track, and I encourage them to keep doing the things that got them there. Or, I let them know that they still have some work to do. And then I work with them over time to address the issues that will help get them there.

Too Much Detail?

Going back to the plan I presented last week, the planning software told me that with "average returns" on their portfolio, my clients would be able to fund 95 percent of their goals, 87 percent if they were victims of "bad timing." The Monte Carlo analysis let us know that their "likelihood of success" was 81 percent. While those numbers are important for me to understand as their planner, I don't think they help the client. There is no way that we can project what their lives will look like years into the future with anything that comes close to this kind of precision.

While I certainly believe that helping a client work through a retirement projection is important, I also believe that the level of detail that many of us provide in the plan can do them a disservice.

As planners, it's important for us to understand the technical issues: the "4 percent rule;" how a Monte Carlo analysis works and what it tells us; how the latest changes in Social Security claiming strategies can affect a plan; and how the risk/reward profile of various asset allocations can increase or decrease the plan's likelihood of success. This is where the true value of publications like the *Journal of Financial Planning*, other industry publications, and the FPA Knowledge Circles help. We get a chance to share, discuss, and learn the latest studies, theories, and trends in the academic world of planning.

Sometimes planners pride themselves on the quality and visual impact of the plans they present. But that's not what our clients want to see. I liken it to a visit with my doctor. I don't want to know the chemistry and biology that goes into my bloodwork analysis. I don't want to see the charts that show my "likelihood of success" of living to a ripe old age based on the current state of my health. I want my doctor to apply her knowledge and experience and guide me through making the right health care choices so that I can have the best health outcome possible. My clients want me to use my knowledge and experience to help them make the right financial choices so that they have the best financial outcome possible.

While it sounds good in theory, clients don't decide to spend 4 percent of their portfolio this year and then adjust that spending the following year by the rate of inflation. They may, after some prodding and guidance from their adviser, set some specific goals, but those goals are usually very elastic. Today they may be very clear and excited about their goal to travel to Europe every year. But life changes and those goals will change. Next year, they may decide to remodel the kitchen. The inputs that we use today when building a plan for a client will change dramatically as the years roll by. Life happens.

Not a Plan, a Road Map

I also believe that this is where we can add the real value for our clients. We should work with them to develop a framework for the life that they want to live. Their plan should resemble a road map of sorts. But as they travel along that road, there will be lots of turns and maybe even some detours that we didn't see coming. With good planning, we can help the client plan for the best, but prepare for the worst. And the plan must be flexible. What happens if one spouse becomes disabled or passes away prematurely? What about a job loss? What about a positive event, like an unexpected inheritance or a lucrative career change?

We should work with our clients to plan for a great retirement and help them make good financial decisions as they go through the various transitions that life brings on their journey. But I think we should be very careful about the specificity we use when going over the details with them. We need to help them understand that the plan that they see today will more than likely be far different from the reality that will be their life. ■

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