

## *When You're Serious...*

by Bradley R. Newman, CFP®

### **It's Not What You Pay But What You Keep**

#### Who says all Fees are bad?

With the impending implementation of new fee disclosure requirements for qualified retirement plans set to roll out in August, there has been a barrage of news stories and interviews that focus on fee reduction. While nobody likes overpaying for goods and services, there are instances when a higher fee, within reason, may not be the worst thing for you. In the investment world, as opposed to having a singular focus on what your costs are, it is more appropriate to focus on what you keep at the end of the day; i.e., total return net of fees.

#### Not all fees are created equal

For the record, you need to have a very clear understanding of what you are paying in fees and what you are getting in return for each fee. There are some fees that have an opportunity to add value for you; for instance, the fee paid to the manager of a mutual fund. Assuming that the fund manager is doing his/her job, the fee they receive to manage your money is an example of good fee. On the other hand, sales and marketing charges do not add direct value to the management and performance of your portfolio and should be eliminated whenever possible or at least minimized. It is imperative to have a clear understanding of what fees you are being charged and what the

purpose of each fee is before you can begin to make judgments regarding their appropriateness.

#### What can't I see?

Not all fees will be clearly spelled out for you. There are some fees that are structured as an 'up-front fee', like a commission or a sales charge. However, many fees are imbedded inside of a mutual fund, or other investment, and structured to be paid out of investment gains; this net-return structure becomes much harder for you to quantify. When your fees are not presented to you in a clearly itemized fashion, it doesn't mean that you aren't paying them. You need to understand that there are costs associated with every investment, and while it is harder to find the fees that are netted out of performance they are still having an impact on your bottom-line returns.

#### Is there value?

For most investors, the visceral instinct is to choose the investment with the lowest level of fees, or at least the lowest level of fees that they can identify. A question to continually ask yourself: "Is there any value to be had for choosing an investment with a higher fee?" As an example, let's compare the fees to the net returns of two large cap value funds; one is a Vanguard fund and the other a Nuveen fund. Both funds have the same investment mandate as large cap value funds, but the Vanguard expense ratio is 0.50% lower at a rate of 0.39% versus the expense ratio of the Nuveen fund at 0.89%. On the surface it would appear that the less expensive Vanguard fund would be the best choice; however, choosing to own the Vanguard fund in 2011 would have cost you 6.4%

or almost \$16,000 on a \$250,000 investment. While the Vanguard fund is less expensive, it lost -4.0% in 2011 while the Nuveen fund gained +2.4 in 2011; the net benefit to your bottom line would have been notable by choosing the more expensive option.

#### Hire an expert

Are you confident that you've identified all of the fees in your investment portfolio? If you are utilizing the lowest cost investments available, are you certain that there are not slightly more expensive options that would provide a better net-return for you? If not, hire an expert to guide you through the process. Specifically, engage a fee-only advisor who will not have conflict of interest based on what fees are associated with the investments that you will hold. A thorough analysis will clearly tell you what you are paying, what you are paying for and the advisory fee might likely pay for itself right up front, as well as on an annual basis for years to come.

*Bradley R. Newman, CFP® is with Roof Advisory Group Inc., an independent investment management and financial advisory firm based in Harrisburg. The firm is a fee-only registered investment adviser that provides portfolio management and financial planning services for individual and institutional clientele. The firm's email address is [invest@roofadvisory.com](mailto:invest@roofadvisory.com)*