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Newsletter Article Reprint

Transition Experts, Financial Planners, Accountants and Money Managers - A Potential Conflict of Interest (by H.M. Smith)

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Recently we've seen Certified Financial Planners and accountants acting as money managers and "Transitions Experts". At least three large firms have entered the practice transitions forum it seems, to manage the proceeds of the sale. In some cases claims are made that the right structure allows taxes to be avoided or deferred to a future date. Taxes cannot be avoided! They may be deferred by using retirement vehicles such as a Defined Benefit Plan, but ultimately you will pay the taxes.

Professional's expertise and their impact in the transition process:

Transition Experts assist you determining the proper transition to enter into as well as facilitating that transition. They are current with tax implications, legal precedents and the market in general. They are not be motivated by your choice of financial planners or money managers. They are paid a commission or fee for the services that they render.

Accountants (CPAs) keep track of money. They do accounting, auditing, tax, and consulting work. Generally they provide tax advice, profit and loss statements and prepare tax returns. They will also represent you should the IRS challenge your tax return. They are generally paid a fee for their professional time.

Money Managers either take a commission for each transaction, take a percentage of the money being managed or are paid a flat fee. In any case, they profit by long term management of your money. Financial Planners evaluate your assets, your liabilities and your income to project the amount of money you will need for retirement and the amount of money you will have when you retire. They try to reconcile the two using actuarial tables that project a reasonable return on your investments and by anticipating your financialneeds from the time you retire until you die.

Financial Planners make money by charging by the hour or by charging a fee for preparing a financial plan. Actuaries review the increase or decrease of assets in the financial plan each year and reproject, using actuarial data, how the plan is tracking. After new projections are determined, the financial planner comes back into the picture to adjust investment strategy to meet the financial plan goals.

Understanding the role of these key professionals in your transition and financial planning is necessary to choose the right advisors. Most knowledgeable attorneys advise that being the financial planner and the money manager is a conflict of interest. Attempting to provide all four services within one firm seriously exposes your transition and your retirement plan to prejudicial advice. Using separate entities affords you an automatic check and balance system which is ultimately in your best fiscal interest.

Example 1
One financial planner recently suggested his client's proceeds go into a Defined Benefit Plan as a tax deferred strategy. Had the client paid taxes on the money at the time of receipt, using appropriate allocations, he would have paid 95% of the purchase price at the capital gains rate of 15% as his total tax. Capital Gains tax is currently the lowest form of taxation. Following the financial planner's advice means the client is taxed at 35% when he takes possession of the Defined Benefit Plan. The $800,000 that was tax deferred ultimately results in an additional $160,000 in taxes. Had the doctor taken his money and paid taxes at the time he sold, the financial planner would not have had the opportunity to manage that money and profit from the fees received for those services.

Example 2
We saw a similar scenario In another recent transaction. The seller was advised to allocate the purchase price so that nearly 100% of the practice sale would be tax deferred. The motive was for the accountant/financial planner to gain control of the proceeds and invest them for "retirement". Again the deferred amount would be eventually taxed at 35% and in this case, the advice totally ignored the financial condition of the seller and his current need for the money to repay existing loans.

Conclusions As in all transactions, "Caveat Emptor" or "Buyer Beware". We strongly recommend finding an ethical transitions expert, a knowledgeable accountant, a good financial planner, who will usually refer you to an actuary, working at arms length and a list of money managers, again arms length, with whom they have worked and are comfortable. This grants you the protections offered by diversity and separation.