Technology Tools for Today

The Oasis Group

UNLOCKING GROWTH OPPORTUNITIES:

The Case for Liability Management in High Net Worth and Ultra High Net Worth Client Portfolios

Sora

Financial Advisors Should Consider Liability Management

Financial advisors have a responsibility to ensure that their clients are achieving the client's financial goals in the most effective manner possible. However, by focusing solely on asset accumulation, financial advisors may be neglecting a crucial aspect of their clients' financial health: their liabilities. It is important that financial advisors expand their services to include liability management, as this will not only benefit their clients but also strengthen their role as the client's trusted advisor for all aspects of the client's financial life.

High and Ultra-High Net Worth clients recognize the benefits of liability management. Ultra-High Net Worth advisors assist their clients in managing their liabilities to produce better outcomes. These include fast access to liquidity, tax deductions on the interest of debt financing, and retaining ownership of assets while leveraging equity within the assets. When financial advisors ignore liabilities, they leave their clients vulnerable to financial strain and missed opportunities. Advisors who want to compete more effectively for this class of clients, liability management advice is critical.

Furthermore, offering liability management services allows financial advisors to differentiate themselves from competitors, such as banks and credit unions, who may offer similar wealth management services but lack the personalized attention and deep financial planning that an independent wealth management firm can provide. By offering a comprehensive suite of services that includes both asset and liability management, financial advisors can cement their position as trusted advisors and build long-lasting relationships with clients.

Why Liability Management Matters

As a financial advisor, it is easy to get caught up in the race to help clients accumulate assets. After all, investing in stocks, bonds, and mutual funds is what most people think of when they hear the word "financial advisor." However, by focusing solely on asset accumulation, many advisors are missing out on a huge opportunity in liability management.

Liability management involves helping clients manage their debts and liabilities, including everything from mortgages, unexpected medical expenses, and credit card balances to student loans and car payments. By offering liability management as part of your wealth management services, you can position yourself as a holistic advisor who is committed to your clients' overall financial well-being, not just their investment performance.

Higher net worth investors understand the value of liability management as a tool to increase their net worth by increasing equity in assets and arbitraging interest rates. Creating equity in a rental property while using the interest and expenses associated with that rental property to reduce taxable income is an excellent example of how a high net worth individual may manage liabilities to their advantage.

Liability Data is Hard to Get

In our current financial landscape, managing debt has become an increasingly complex task for both individuals and financial advisors. Traditional methods of debt management rely heavily on the client's credentials to establish valuable links between their financial institution and their financial advisor, but these methods are not without flaws. These links are fragile and can easily break when the financial firm updates their source systems, the client enables multi-factor authentication for their financial institutions, or the client changes their password. Once the link is broken, the information becomes outdated and significantly less useful.

Financial advisors can ask for insight into their client's debts; however, most advisors don't probe for several reasons:

1. **Most advisor technology cannot effectively track liabilities as they weren't designed to do so.**
2. **Advisors lack the internal processes to capture, organize, and analyze client debt.**
3. **Advisory firm don't possess the document management capabilities or organization to capture and store debt documents.**

Clients are also reluctant to share their entire debt picture due to the effort required to gather their loan statements and upload them to the advisor's client portal. So ultimately, the client's conversation with the advisor is limited to discussing their mortgage and the amount of equity in their primary residence.

The complexities don't end there. The process of debt optimization - gathering prevailing rates from lenders and determining strategies for refinancing, cross-collateralization, and liquidity management - is a task that requires extensive expertise and an inordinate amount of time. Many advisors do not provide this advice often, so they are less confident in their advice. This complexity makes it an unappealing place for advisory firms to go.

Considering these challenges, managing debt has not been a significant revenue generator for advisory firms, outside of securities-based lending or SBLOCs.

SBL & SBLOCs Are Not Liability Management

Securities based lending (SBL) and SBLOCs (Securities Based Line of Credit) are financial tools that provide several benefits to investors. These include increased liquidity, flexibility in managing investment portfolios, and potential tax advantages.

One of the main benefits of securities-based lending is its ability to increase liquidity for investors: by using their existing securities as collateral, investors can obtain loans without having to sell off their assets. This allows them to maintain their investment positions while also accessing cash as needed for other purposes.

In addition, securities-based lending provides flexibility in managing investment portfolios. Investors can use the funds obtained through these loans for a variety of purposes, such as financing new investments or personal expenses. This flexibility allows investors to take advantage of market opportunities and make strategic investment decisions without being limited by their current available cash.

Furthermore, securities-based lending can also offer potential tax advantages. In some cases, the interest paid on these loans may is tax deductible, providing investors with additional savings and benefits.

Overall, securities-based lending and SBLOCs are powerful tools that can help investors better manage their finances and investments. They provide increased liquidity, flexibility, and potential tax advantages, making them a valuable tool for individuals looking to optimize their financial strategies. With careful planning and management, securities-based lending can be a beneficial addition to any investment portfolio.

However, SBL and SBLOCs are traditionally offered by wire houses and large bank custodians; financial advisors need solutions that differentiate their firm from wire house and bank competitors. In addition, these solutions offer liquidity and still avoid the liability conversation.

Risks of Ignoring Liability Conversations

Failure to discuss liabilities carries the consequence of driving their clients to other financial institutions for their lending needs. Established institutions like Bank of America, for example, are more than eager to step in and fill this void. They offer lending solutions and work aggressively to entice clients, not just in lending services, but in transferring assets to their private wealth management arms, such as Merrill Lynch. This comprehensive service is attractive to many clients who prefer the convenience and the integrated approach of such institutions.

The competition is not limited to wire houses, such as Bank of America. Regional and national banks, credit unions, and even custodians compete with financial advisory firms for this business. Schwab Bank, BNY Mellon, and Bank of America are only a few examples of firms who will offer an investor advantageous pricing for mortgage rates.

The risk is even more pronounced when advisors opt to go independent, moving away from full-service wire houses. In such instances, they potentially leave behind clients who value the end-to-end private banking experience these larger institutions provide.

To retain clients and remain competitive, financial advisors must make the shift toward a more comprehensive service model. By covering a full range of financial services, advisors can ensure client loyalty and guard against losing them to larger institutions.

Not All Debt Is Bad

It's crucial to recognize that not all debt carries negative implications. There exist constructive and beneficial uses of debt, and financial advisors have the capacity to provide advice on their client's existing obligations or pinpoint the most suitable new loans for the client's circumstances; in managing debt, don't be too hasty to eliminate it all.

For example, consider the client who has a 30-year fixed mortgage with a 3 percent interest rate and wants to accelerate their mortgage repayment. This might not be the most judicious strategy if the current rate for treasuries is 5 percent.

The value of impartial, professional financial advice for individuals—particularly in contrast to the emotions associated with borrowing and debt—is where expert guidance and coaching can truly make a difference. By conducting a detailed analysis of a client's debt, advisors can create tailored proposals that address their indebtedness. Furthermore, financial advisory firms that are well-equipped to provide ongoing credit management services can position themselves as all-encompassing solutions for the client's financial needs.

A New Approach to Liability Data

The competitors to financial advisors we've reviewed can access a client's credit information using a soft pull of data from the credit agencies. A soft pull does not affect a credit rating. This is completed via an application programming interface (API) query to the credit agencies. The soft pull will return a limited credit report and FICO score. While these results are useful to check consumer credit to understand creditworthiness and prequalify customers for loans, it does not provide the level of information that an advisor would need to provide actionable financial advice. This set of data lists all the client's liabilities, including mortgages, credit cards, auto loans, student loans, personal loans, and personal lines of credit.

Additional information can enable the financial advisor to have next best action conversations, such as the interest rate and current balance. Sora Finance can enrich the data from the soft pull of the client's credit report. Their data enrichment process leverages APIs directly with the lenders to get additional information, such as the loan interest rate and balance, without requiring the client to log in and refresh the data from the lender each month. The API also returns the term of the liability, up to date balance, and monthly payment amount.

Their API requires the name, social security number, phone number, address, and date of birth of the client. This seamless process arms the financial advisor with the information that they need to have more effective conversations with the client about their liabilities and to provide timely financial advice.

Sora Finance leverages a set of APIs that they have developed to gather Automated Valuation Models (AVMs) for the client's property. This is a similar technology that Zillow and Redfin use for marketing purposes to calculate the property's valuation. Sora Finance can pull AVM information beyond the simple valuation and at the same level that mortgage lenders use to determine the appraisal value of the home.

This lender level of data puts the financial advisor on par with their bank and credit union competitors. It enables the financial advisor to thoroughly evaluate the liabilities of their client and drive insightful advice.

Better Liabilities Data Leads to Better Conversations

Financial advisors who leverage better liability data can have more insightful conversations with their clients, for example:

- Refinance high interest debt, such as credit cards, with lower interest or fixed-rate debt options.
- For new loans, the data combined with credit score and income allow Sora to scan its robust lender ecosystem to identify the best offer and ensure a more seamless loan execution.
- Leverage the interest rate savings from refinancing to increase investment savings and better prepare for retirement.
- Consider a cash out refinancing option to eliminate high or fluctuating interest rate loans in favor of a lower fixed-rate mortgage.

Advisors, through their proactive approach, can assist clients in optimizing their existing debt portfolios and guide them while acquiring new loans. This active engagement results in better decision making when it comes to selecting new loans.

Clients benefit by engaging the services of a financial advisor, clients can enhance their FICO score significantly and preserve this improvement over the long term. This advantageous move doesn't merely pave the way for favorable loan conditions in the future but also bolsters the prospects of securing premium insurance rates and increases the likelihood of successful applications when seeking rental accommodation, among other benefits.

Finally, let's address one of the most crucial aspects of financial advisory — client relationships. We discussed how many high earning clients are living paycheck to paycheck earlier in this paper. The ability to help this segment of high earning clients will significantly deepen the client relationship and elevate the firm from financial advisor to the client's trusted advisor.

Advisors with better liability information can help clients on their journey to accumulate assets by helping those same clients effectively manage their liabilities. By discussing liabilities and recommending next best actions, advisors can deepen their relationships with existing clients. This level of involvement goes beyond transactional interactions, solidifying the advisor's role as a trusted and valued partner in their client's financial journey.

Liability Management to Drive Growth

In today's highly competitive financial advice marketplace, clients demand and expect a comprehensive, full-service advisory experience. Loan and credit management were services expected by 83 percent of wealthy investors and only 3 percent of financial advisors provided this service. Therefore, the wealth management firm who offers liability management services to their clients is already differentiated from their competitors.

Financial plans that include liability management can help to qualify a perspective client. For example, a potential client with a large potential IRA rollover who is nearing their distribution years may be considered a great prospect. However, that same prospect with significant liabilities has a very different net worth and may be viewed differently.

Numerous advisory firms are setting their sights higher, specifically targeting ultra-high net worth clients. These wealthier families frequently leverage debt as a strategic tool for a variety of purposes, including the effective management of tax liabilities. Accordingly, it is imperative for financial advisors to have (1) access to a robust platform that allows them to attract HNW and UHNW clients and effectively manage their complex financial scenarios.

Financial plans that include liability management can also lead to higher conversion rates. As we discussed, 83 percent of wealthy investors expect loan and credit management services. Offering those services can lead to a higher conversion rate for prospective investors.

The Time to Offer Liability Management is Now

Clients and prospects need and desperately want their financial advisors to look beyond the assets side of their balance sheet and help them to focus on their liabilities.

Financial advisors in the past were hindered by the lack of access to timely, reliable, and easy to obtain liability data for their clients. Advancements in technology, like Sora Finance's platform, enable financial advisors to compete with banks, wire houses, and credit unions more effectively by providing them with better data.

Financial advisory firms can deepen client relationships, win prospects who are interested in liability management, differentiate themselves from their competition, and attract new AUM by offering liability management services. The authors hope that more financial advisory firms capitalize on this opportunity.

(1) Wealth Management Redefined; Spectrem Group; https://spectrem.com/Content_Product/redefined-wealth-management.aspx.

The Oasis Group

John O'Connell
The Oasis Group

Technology Tools for Today

Joel Bruckenstein
Technology Tools for Today

Sora

Rohit Agarwal
Sora Finance

Sora

Siddhartha Oza
Sora Finance