Financial Planning for Management Consultants:

7 key questions you need to answer

Authors: Adam Walkom & Adrian Johnson
Permanent Wealth Partners
Financial Planning. For Professionals. By Professionals

PERMANENT
WEALTH PARTNERS

What is unique about you?

To be honest – a lot. You work very hard. You're obviously smart and you know your value. You also have the capacity to earn very well. However, earning and long-term wealth often have little to no correlation. Why? Because what do you do with the funds really matters.

Does any of this sound familiar..

- You are too busy working so you just let the cash build up assuming that there's nothing wrong with that.
- You feel like you earn well but the costs of living just stop you from putting any money away in a planned way.
- You know that pensions are important, but you have no idea what yours is really doing.

Well, if any or all of those apply to you, I've got some good news.

We work with a number of Management Consultants from a range of firms – top tier to self-employed. Whilst each individual's financial situation is unique, the characteristics of both Management Consultants and their roles give us specific intelligence and information across this cadre of professionals. This discussion document looks to highlight some of these common issues this group faces and specifies the unique decisions each individual should be making.

What is unique about Management Consultants?

From the outside the life of the Management Consultant may seem very slow and relaxed, even staid. Picture Marvin Bower (McKinsey) or Bruce Henderson (BCG) and you get the vision of studied, deepthinking men in suits. The reality we all know is a lot different than the perception. International teams from all backgrounds in age, race and gender working together under significant time pressure to produce extraordinary results for their clients. The pressures are much higher than "normal" jobs, but so are the rewards. That's what makes it so difficult to get into some of the top tier consulting firms in the first place. Most firms operate an "up or out" policy so you find there will always be opportunities – whether you agree or not – to leave the firm and take up employment elsewhere.

Each firm has their specific remuneration structures and opportunities – whether it is to participate in internal private equity placements or simply buying your employer's stock at a discount – and these have specific implications on tax and planning needs.

What makes this industry unique though is the relatively shortterm nature of each employment. Due to the high-pressure demands on the role – time pressures and travel as the top two we hear - for a lot of the top tier consultants, retiring at 67 when they receive their state pension is highly, highly unlikely. Most consultants look forward to a second phase of their career, still doing meaningful work but without the pressure and potentially lower rewards. This tends to mean that the "earning phase" of most management consultants career, the most important part of building their overall lifetime wealth, is also the busiest and most stressed where important non-work decisions can be put on the back burner. We urge you not to make your own financial planning one of these delayed decisions. When consultants are being paid very well and saving more than they ever have, there can be a strong tendency to be complacent, to think "we've got enough cash" and leave it at that. Don't be that person who looks up in 10 years' time and thinks "where did it all go?" Making a certain number of decisions today, with your potential earnings capacity, can almost guarantee you and your family's financial future. Does that sound like a good trade-off to you?

Key question 1

Can you construct your investments more efficiently?

You pay a lot of tax. Do we need to remind you? As most probably an additional rate taxpayer, not only do you pay the top-rate of tax of 45% but you also lose out on your personal allowance (the first £12,500 of income is tax-free for most others), but then you also have to pay back child benefit amongst a number of other stealth taxes that hit the higher earners.

The bonus figure on the piece of paper that is passed to you is never what you receive because of tax that needs to be taken out.

Gross earnings of £600,000 per year means you will end up paying £271,722 of that in tax [1].

Tax is law. But then so is getting tax relief. Everyone complains about paying taxes, but many don't actually fully utilise all the different tax reliefs available to them. Do you? There can be significant savings to be made by structuring your earnings and investments in a tax-efficient manner. There are many different financial products with different tax treatments – we review a few below - that can all have a place in your overall asset holdings picture as long as they suit your specific situation. Here is a brief summary of some of the options you can consider:

1 ***based on the 2023/24 tax rules.***

Can you construct your investments more efficiently? *continued*

Investment Savings Accounts (ISAs) in the various forms are very efficient tax wrappers, with no tax payable in income or dividends. Neither do you pay capital gains tax on investments held in an ISA; for investment outside an ISA, there's currently a £6,000 allowance after which gains are taxed at 20% (28% for residential property).

How efficiently have you constructed your investment holdings to minimise taxes and maximise growth?

Venture Capital Trusts (VCTs) let you access attractive tax reliefs as an incentive to take on the risk of backing early-stage businesses. Investors can claim upfront tax relief equal to 30% of their investment on the first £200,000 invested each year. Dividends and capital gains are also tax-free.

Enterprise Investment Schemes (EIS) are tax-optimised and attractive investments for investors who are comfortable with higher risk. Here, you can back early-stage companies and access a number of valuable tax reliefs including upfront income tax relief, tax-free capital gains, capital gains tax deferral, and inheritance tax relief.

Seed Enterprise Investment Scheme (SEIS) structures are similar and offer substantial tax benefits for investors who are prepared to take some risk investing into smaller unquoted trading companies, all of which can be considered in the optimised portfolio.

Key question
2

How much of my overall wealth do I want linked to my employer?

How reliant financially are you on the sustainability of your employer? Most people don't realise how reliant they really are. If you're like most people we talk to, then your employer is responsible for the following:

Have you considered how much of your financial wellbeing is reliant on your employer?

Your pension contributions

Your pension management

Your life insurance

Your health insurance

Your income protection

Your car allowance

Your gym membership

Your childcare vouchers

And when you think about this list above, note the one thing I didn't even mention – Salary.

It's when people understand how intrinsically intertwined their financial livelihoods are with their employer, that we like to gently question whether some diversification may make sense?

Also, this does not include the private equity opportunities or discounted equity you may be able to purchase separately. Whilst the psychological appeal of limited opportunities is always strong, we regularly like to play devil's advocate with our clients. What if things went bad? How can we de-risk this is much as possible whilst still getting access to the upside. These are the sort of discussions we regularly have with our clients.

Key question 3

When are you going to stop?

To become a partner at a management consulting firm is a very big deal. You have worked very, very hard to get where you are and you deserve the stature and remuneration that being a Partner provides. But have you ever stopped or even slightly paused to ask “What’s next?” I’m sure most people do not plan to die at their desks, so planning for life beyond consulting is a crucial step. Especially when you, with a little bit of planning, will have the financial resources to do exactly what you want to do.

A little side story – the BBC pension scheme used to be the most well-funded pension scheme in the U.K. [2] Why? Because if you think what journalists and newsrooms used to be like from the 1930s upto the 1990s, they were hard-working, hard-drinking, hard - smoking places. There were a significant number of journalists (mostly male) who would retire at aged 60 (if they even made it that far), get their gold watch and be dead 5 years later. The pension scheme was all set to pay out for the rest of the normal life expectancy and would rarely have to. Times have changed considerably since then and now with life expectancy increasing every year, there is every chance you will need to live of your pension assets for 30+ years.

2 https://www.ftadviser.com/pensions/2017/08/23/bbc-to-pay-340m-to-fund-pension-scheme/

Key question
3

When are you going to stop? *continued*

For a number of Partners, they key consideration is not necessarily thinking about retirement, but thinking about when they can stop working or step-down to a simpler role. A lot of people want to know "their number" as in, based on certain calculations, at what age can they do this and still have enough assets and income to last the rest of their lives. Speaking to someone formally around this can prompt a lot of thinking and should be not necessarily a one-off conversation, but an evolving discussion that takes place over many years as the situation develops.

How thoroughly have you ever thought about, at the bottom of your heart, what is truly important to you?

Good financial advisers will even build financial models for their clients to have this discussion. Going through process of building the model and setting the assumptions provides invaluable discussion and thinking time for partners to work out what is important to them in their post-practice work.

Working backwards is sometimes a strategy used by advisers to prompt this conversation. Again, good advisers will do this and ask questions such as "What will you be doing in 20 years' time? Where are you? What does your house cost? How much are you spending every month?" Then working backwards from there to work out the cost of the sustainability of that lifestyle and what is required at the outset to achieve it.

Key question 4

How much would you pay to remove the worst case scenarios?

What would be the financial implications to your family if you were hit by a bus tomorrow?

Something would have to go very wrong for you and your family not to be financially comfortable for the rest of your life. The problem is, sometimes bad things just happen.

The good news is, for a small cost each month, you can effectively offset two of the worst case scenarios – death and long-term illness. You will have group life cover through your employer, but will that be enough? Group life schemes tend to operate within pension tax structures and are subject to changes in regulation in this area. Have you thought about how much you (or more relevantly your family) would need if you were no longer around? Or permanently incapacitated.

Perhaps the easier thinking is done more around estate planning. Simply having a will in place is the most powerful first step. You would be amazed at the number of people who don't have this in place. Lasting powers of attorney are also important to enable decisions to be made in your interest should you not be able to. From an asset perspective, your adviser will help structure your assets in the most efficient way so they can be passed down to the next generation or to your philanthropic choices.

Delaying or shirking these tough decisions can bring a huge amount of unnecessary grief on your family at the worst possible time. Don't be that person.

What type of investor are you?

Even if your sole financial asset, other than the cash in your bank account, is your pension you are either explicitly or implicitly choosing between being an active or passive investor.

An active investor is one who is regularly making decisions about investments and commits time and resources to researching and executing purchases and sales in various assets. There is an assumption built into the active investor which is that they can consistently beat the market over time.

A passive investor is one that generally is comfortable with the average return of the market and as such does not spend the time and resources buying and selling (being active in the market), but rather buys and holds. The proliferation of index funds and exchange traded funds ("ETFs") has made taking this approach very straightforward for all levels and types of market participants and also made it very cheap to do so.

It is true that considerable debate still rages about the case for active fund management and active investing; but if you believe that you can consistently beat the market, we would submit that:

- You are ignoring an overwhelming amount of empirical evidence on the subject;
- In the wrong profession, because your extraordinarily rare talents would be better rewarded in a hedge fund; or
- That you are probably incorrect.

Passive investing does not simply rely on making some bets and letting things take care of themselves. Intelligent passive investing requires proper portfolio construction and regular review to ensure

that the portfolio is performing to your individual needs.

Key question
5

What type of investor are you?

continued

How much of your portfolio will you put at risk?

Have you objectively evaluated your risk tolerance, capacity for loss and calibrated the amount of investment risk you are prepared to embrace across the various time frames in your investment portfolio to ensure your money is working as hard for you as you did to earn it?

We know from talking to our clients who are Management Consultants that sometimes you will have restrictions on buying certain companies. At the same time, you potentially will be offered private investments through your firm. How do these restrictions and opportunities fit within your overall portfolio? Are they calibrated appropriately?

What assets or asset classes should you invest in?

When looking to make investments have you given full consideration to the structures from a tax perspective, from a cost perspective and a risk perspective to ensure you are optimising to achieve maximum growth?

Are investment decisions based upon independent advice from the whole market to take account of the try suitability to your specific circumstances?

Do you conduct detailed research on an ongoing basis to ensure that you understand the opportunity and risk of any specific investment offers?

Portfolio construction takes into account all of factors that are personal to your circumstances and looks forward to the vision, goals and objectives you lay out then sets about finding the optimal bespoke portfolio of investments that works for you.

How much thinking do you want to do on this?

Key question

6

Have you thought about your pension recently?

There is another stealth tax put that impacts just the higher earners in society. Once you have gross earnings above £360,000 then HMRC caps the amount you can put tax-effectively into your pension to just £10,000. If you earn just below this figure then there is a sliding scale in terms of the calculation required to ascertain the correct limit. Many partners end up completely opting out altogether of their employer pension scheme and receive the contracted pension contribution due to them as part of their PAYE compensation. This may not always be the best idea for a number of reasons, however it tends to be common practice.

How well do you understand your pension scheme (or schemes) and are you maximising the growth potential?

The problem with this is that sometimes this pension just then gets forgotten about. Pensions are one of the most tax effective investment vehicles available to anyone, however even more so for higher earners. There are limits both in terms of contributions and total sum involved, but any balances below these should be maximised in terms of their potential tax-efficient growth opportunities. Yet, what we see so regularly is the annual pension statement arrives once per year, is briefly looked at to see growth (or not) and then discarded with other papers to the draw to be filed.

Realistically if you are unlikely to access the funds from your pension for greater than 10 years, you do not need any bond or property exposure (as you have that already through your home) and it should be 100% equity tracker funds and growth focused. Because of your income (and not needing to touch it) you can easily ride out any bear markets with the trade-off being much better growth in the long-term because of this.

Should you work with an independent adviser?

In this quote from his essay “Advice to a Young Tradesman” back in 1748 Benjamin Franklin was essentially conveying the opportunity cost of laziness. The modern aphorism “Time is Money” is now usually associated with the “work harder, work longer hours, earn more money“ paradigm beset so many professionals, and could hardly be more empirically supported than by the consulting profession charging by the hour...but how much time do you spend working on your money?

Your clients come to you for assistance in vitally important matters where they do not have the domain knowledge, experience and skills necessary to get a good outcome.

Sure, they might be able to figure some of it out for themselves, they might be able to scrap together some time in amongst their other commitments, they may be able to rely on advice from friends; BUT, when in your experience does that path outperform hiring an expert?

Working with a professional adviser for your personal finance means you have a sounding block, coach, consultant and sage. They help you see opportunities and risks you may have missed and make sure you stay on the right track to achieve your complete independence. They save you considerable time in administration work and absolute clarity in terms of your current and future financial situation. In short, working with a professional adviser should provide you with a sense of profound financial peace.

PERMANENT
WEALTH PARTNERS

About the Authors

Adam Walkom was a Consultant with McKinsey & Company in their Melbourne office. He also has previously worked on the trading floor with both BNP Paribas and UBS. He became a qualified financial planner in 2014 and now is a Partner at Permanent Wealth Partners.

Adrian Johnson was a Managing Director in Compliance & Regulatory Consulting at Duff & Phelps (now Kroll). Previously he led finance departments at fund management and real estate firms. He qualified as a financial adviser in 2021 and is a Partner at Permanent Wealth Partners.

PERMANENT

WEALTH PARTNERS

Permanent Wealth Partners is a specialist firm of financial planners, focusing on the needs of career professionals. All their financial planners have specific experience in management consulting, asset management, hedge funds and banking.

Financial Planning. For Professionals. By Professionals

To arrange a consultation please contact

hello@permanentwealth.co.uk

or call the office on

0203 928 0950