

TILLY'S GUIDE TO

Smart Investing



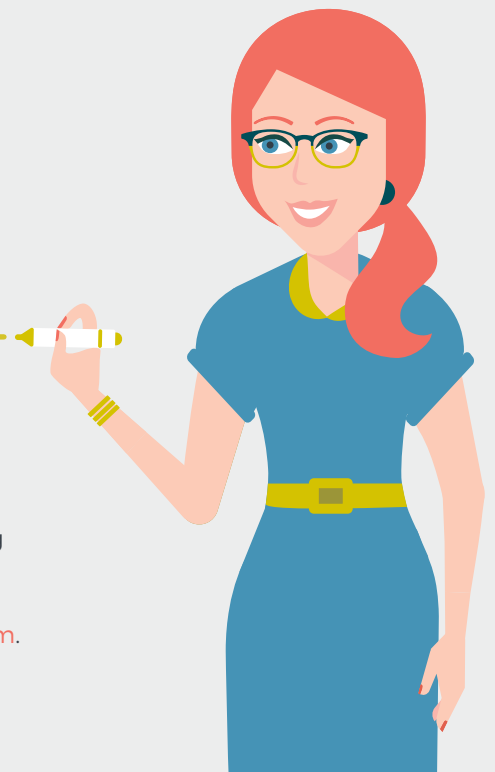
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Tilly's Guide to Smart Investing

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About Tilly

At Tilly, we believe that financial advice should be affordable, accessible, and simple to manage. That's why we are revolutionizing the way you work with an experienced financial advisor, saving our clients both money and hassle. Learn more about Tilly at asktilly.com.



“Investing is not nearly as difficult as it looks. Successful investing involves doing a few things right and avoiding serious mistakes.”

– John Bogle, founder of Vanguard

We at Tilly agree with the great John Bogle. You do NOT need to be an experienced investor to succeed managing your wealth. Gaining incremental knowledge over a long-period of time is a lifelong hobby that doesn't have to be a “job” – but instead it should be an enjoyable journey. The process in learning about the financial world can be fun – like a gratifying challenge.

But before beginning your financial journey, you do need to understand how investments work. For example, what are some of the big mistakes that new investors make and how can I avoid them? How do money management firms earn money? How can I ensure I'm not overpaying for services? What are the various types of investments and how do they work?

We are confident our guide will help you along the way. Enjoy!

You should be knowledgeable enough about investing to make an informed and thoughtful decision.



Tip 1: Choose A Solid Company to Take Custody of Your Assets

"In ourselves, our safety must be sought,
By our own right hand, it must be wrought."

- William Wordsworth

The most important step when investing is ensuring your money is safely kept and not fraudulently taken away from you. Whenever you send your money to an organization, can you trust them with it? Do they have safeguards, insurance, and other protections against fraud and theft? Is your money invested where their online platform says it is?

Custody is the safekeeping of your assets. We recommend that a large, trusted, regulated organization maintain custody of your assets.

The Bernie Madoff fraud scandal was partly caused by the fact that Madoff himself, just one individual, had custody of client assets. As it turned out, the investors' money was not invested as the statements reported; it was elsewhere. So, an important learning from the Madoff case is that just because a "statement" says a transaction occurred, does not mean that it in fact did. It just means someone said it did.

People are often overwhelmed by which asset custody firm to work with. Don't be. Well-known custody firm platforms are similar and will likely provide what you need at a good price. Schwab, Vanguard, Fidelity, TD AmeriTrade, MerrillEdge, and E*Trade are examples of large, heavily-regulated firms that custody assets. Key factors when comparing them include:

- Safety and soundness
- The ease-of-use and features of their platform
- Services and support
- Fees for trading and maintaining accounts

Here is a helpful article comparing custody firms:

<https://www.stockbrokers.com/guides/online-stock-brokers>

Once you have an investment account established, purchasing a mutual fund, stock, bond, or other securities is easy to do. Step one is make sure your account has adequate cash — step two is find the security you'd like to purchase — and step three is to select "purchase" and follow the steps. Most platforms offer educational videos to help you navigate and learn the system.

Tip 2: Understand How Much it Costs to Invest

"Any fool can know.
The point is to understand."
- Albert Einstein

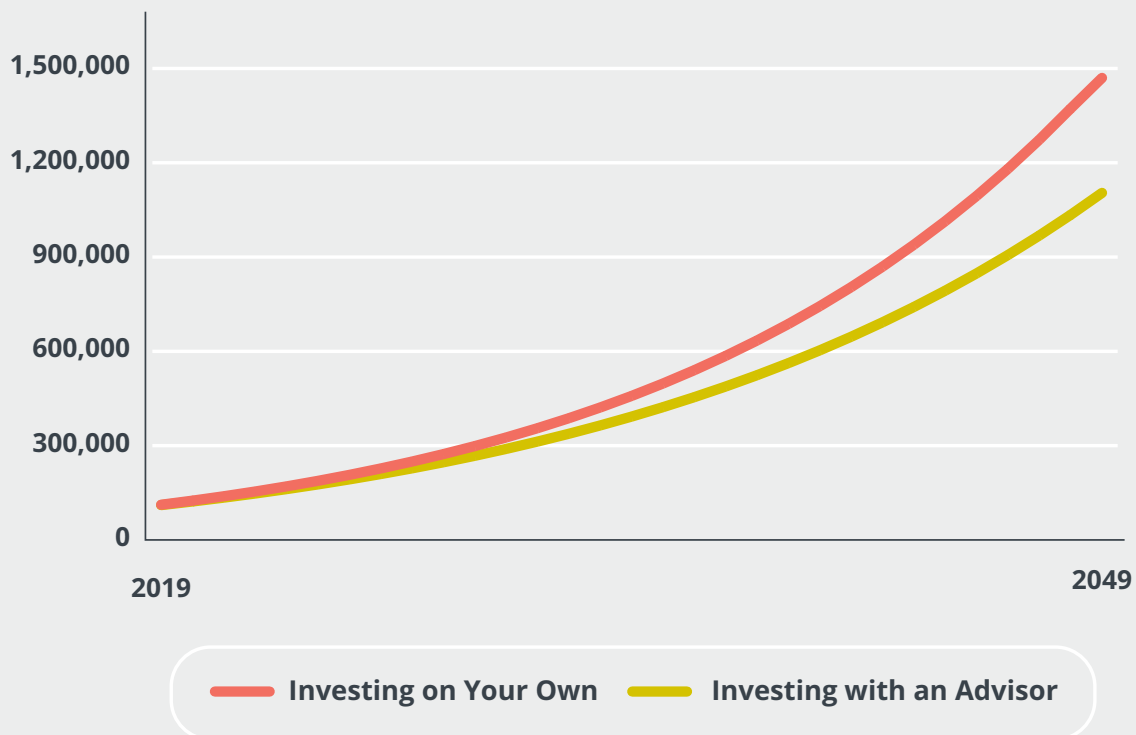
Let's assume you're considering hiring an advisor under the following assumptions:

- 35 years old
- Begin with \$100,000 worth of investments
- Invest \$5,000 per year for 30 years
- Investments earn 7% per year
- Pay 1.25% per year for advice

Over thirty years, the time value of these fees come to \$365,837. Keep in mind, the \$365,837 DOES NOT include fees charged by mutual funds or commissions to brokers. You can just add those fees to the total. Why are the fees so large? Because over a long period of time, 30 years, 1.25% annually really adds up!

The difference, \$365,837 saved over those 30 years by not paying for advice, is a LOT of money!

Managing Investments On Your Own



One reason the investment advisory business is so profitable is because most people don't understand how industry firms charge for services. Investment fees are collected in a similar manner as your paycheck's tax withholdings: They're automatically deducted from your account. And because people don't write a check for those advisory services, they just let it go – and rarely consider these automatically deducted fees as “real” money. But make no mistake about it: The fees deducted are real money – real money you'll need during retirement, to pay for your children's college, or for a down payment for a second home.

A common phrase we hear at Tilly is: “I have no idea how much I'm paying because it's too complicated.” Calculating how much you pay for investments is somewhat complicated, but not too complicated.

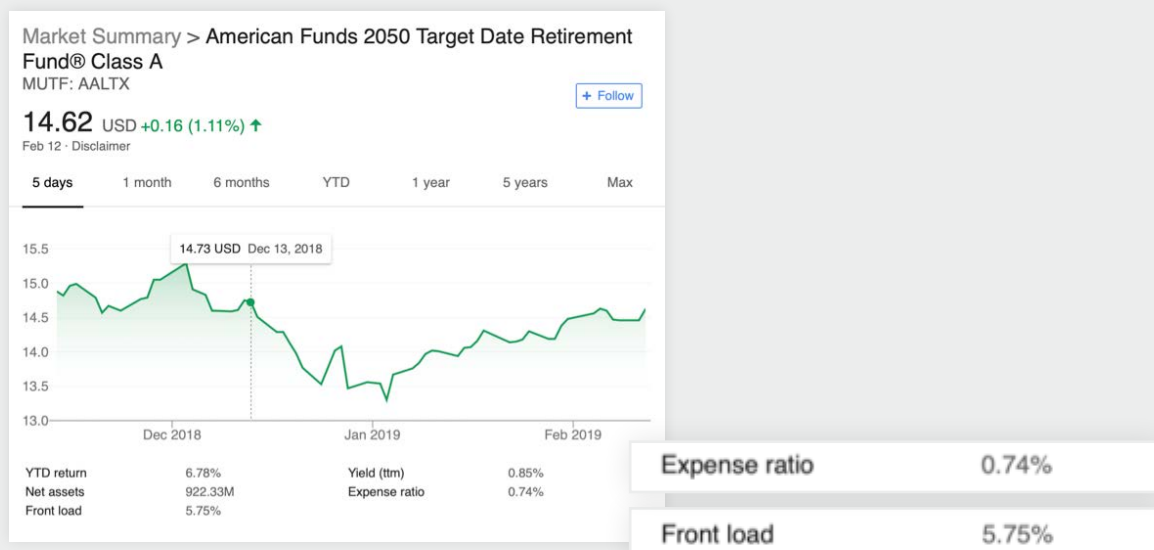
“I have no idea how much I'm paying because it's too complicated.”

Here are the basic fees you need to understand. Keep in mind that even if you're investing on your own, some of them are still relevant.

- **Management or advisory fees:** These fees are only relevant if you hire an investment advisor. The fees are subtracted from your account each quarter. To find out if your “financial advisor” is registered as an investment advisor, as a broker, or both, go to <https://brokercheck.finra.org> and search for your advisor. Just beneath his or her name, you'll see a B, IA, or both. If you see an IA, he or she is an investment advisor and may charge advisory fees. If you see a B, he or she is a broker and may charge you commissions and other fees. If you see both IA and B, he or she can charge you both as an advisor and as a broker. (PS – Be careful hiring someone is both an advisor and a broker; this may be a conflict of interest.)
- **Annual expenses charged by mutual funds:** These fees are subtracted from your returns within a mutual fund and used to pay for management, commissions to your advisor, marketing, and other expenses. They are referred to as expense “ratios” because they are stated as a percentage of the amount you own in the fund. For example, if the expense ratio is 1.0% and you have \$100,000 in the fund, then you're paying \$1,000 per year. These fees range widely depending upon whether the mutual fund is “actively managed” or “passively managed.” (See below for more detail on the difference.)

- **Sales loads/shareholder fees charged by mutual funds:** “Loads” are lumpsum amounts you pay either when you buy or sell a fund. These can be quite expensive. For example, if you purchase a fund for \$100,000 and the upfront load is 5%, then you’re paying \$5,000 either up front or when you sell! If you invest frequently, these loads can really add up, so try to find mutual funds that don’t charge loads but get the same performance over a long period of time.
- **Trading fees, transaction fees, maintenance fees, recordkeeping fees, commissions, wire transfer fees, and other fees:** These costs can add up quickly so include them in your calculation. They are normally printed on your monthly statements or revealed on the broker/dealer’s website.
- **Mark-ups:** If you’re trading bonds, you may be paying your broker a mark-up. For example, if your broker buys the bond for \$1.00 each, he or she may sell it to you for \$1.05 each. Or they may be charging commissions.

If your financial advisor or broker doesn’t provide you with this type of detailed fee information, you can calculate it yourself. Advisory fees, if applicable, are almost always printed on your quarterly statements as “fees” and are deductions from your account balances. These fees are relatively easy to find. Mutual fund fees are rarely printed on your statements; however, you can easily find them by searching the mutual fund’s symbol on the web. For example, American Funds 2050 Target Date Retirement Fund Class A’s symbol is AALTX. If you searched AALTX, it would return something like this:



If this result doesn't come up, you'll see links to the fund summary where you can get the same information. For this fund, you can see the front-end load is 5.75%, and the annual expense ratio is 0.74%.

Here is an example calculation using the following assumptions:

- Your provider is a registered advisor charging 1.25% of assets under management per year.
- You have \$300,000 invested into AALTX.
- You contribute \$5,000 per year to AALTX.

| TYPE OF FEE | AMOUNT INVESTED | CALCULATION | FEES PAID PER YEAR |
|--|-----------------|-------------|--------------------|
| Annual advisor fees | \$300,000 | 1.25% | \$3,750 |
| Annual mutual fund expense (AALTX) | \$300,000 | 0.74% | \$2,220 |
| Upfront loads on new contributions (AALTX) | \$5,000 | 5.75% | \$287.50 |
| Other fees | | | \$300 |
| TOTAL FEES PER YEAR | | | \$6,557.50 |

Normally, you'd have multiple mutual funds with various annual expenses and loads. However, the calculation isn't difficult and only requires simple arithmetic.

This calculation assumes that your provider is registered as both an advisor and a broker. Nearly 2/3 of providers are "duly registered" which means he or she receives compensation from both you (\$3,750 in the above example) and the investment firms that hold your investments (mutual fund expenses in the above example). If your provider is "fee only," this means he or she is only registered as an advisor and does not receive fees from mutual fund companies. Fee only advisors often help you find lower-cost investment options. (See below: Invest passively unless you have expertise.)

Tip 3: Invest In “Passive” Mutual Funds

“I have good news for these non-professionals: The typical investor doesn't need this skill*... Just invest your funds in a low-fee index fund tracking a broad cross-section of businesses.”

– Warren Buffett's 2013 letter to Berkshire Hathaway's shareholders

*“This skill” Buffett is referring to is selecting the best investment.

In 2017, there were 9,356 different mutual funds to choose from, so it's easy to become overwhelmed. But an important thing to know is that there are two main types of mutual funds: passive mutual funds and actively managed mutual funds.

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Passive mutual fund returns track with a market index such as the S&P 500 Stock Index, Russell 2000 Stock Index, or other indices. Actively managed mutual funds have staff who research and investigate which stocks to buy or sell within a mutual fund.

Passive investing is less expensive to manage than active investing because no selection process is necessary. For example, Schwab's S&P 500 Index Fund (SWPPX), a passive fund, has an annual expense ratio of only 0.02% with no upfront loads. But the American Fund (AALTX), an actively managed fund, charges 0.78% with a 5.75% load.

In terms of dollars, if you invest \$100,000, the passive fund would cost you \$200 per year, but the actively managed fund would cost you \$780 per year and each time you invest additional dollars, you'd pay 5.75% as well.

Vanguard's founder was a pioneer of passive investing.

Vanguard's founder, the late Jack Bogle, was a pioneer of passive investing. He pointed out that over the long-haul, these lower-cost index funds almost always beat the returns of actively managed funds.

The chart below shows that during a 15-year period, only 7.57% of large cap "actively managed" funds outperformed the S&P 500 Index. Therefore, if you invest in a "passively managed" S&P 500 Index Fund, you'll pay less fess and likely have better returns.

Report 1: Percentage of U.S. Equity Funds Outperformed by Benchmarks

| FUND CATEGORY | COMPARISON INDEX | 1-YEAR (%) | 3-YEAR (%) | 5-YEAR (%) | 10-YEAR (%) | 15-YEAR (%) |
|---------------------|--------------------|------------|------------|------------|-------------|--------------|
| All Domestic Funds | S&P Composite 1500 | 57.98 | 82.12 | 80.13 | 85.93 | 83.76 |
| All Large-Cap Funds | S&P 500 | 63.46 | 78.64 | 76.49 | 89.15 | 92.43 |
| All Mid-Cap Funds | S&P MidCap 400 | 54.18 | 83.28 | 81.74 | 92.68 | 95.13 |
| All Small-Cap Funds | S&P SmallCap 600 | 72.88 | 93.59 | 92.90 | 93.36 | 97.70 |

Source/credit: <http://www.aei.org/publication/a-tribute-to-john-bogle-with-some-charts-and-quotations/>

If you invest on your own, should you only invest passively? Maybe, maybe not. Depending upon your risk appetite, you may occasionally want to select and purchase some individual stocks or bonds. For example, let's say someone invests a portion of his assets into undervalued "micro" stocks (companies valued at more than \$50 million and less than \$300 million). He enjoys learning about these companies and has the risk tolerance to weather their ups and downs. This approach is fine so long as you don't bet a large portion of your overall assets, do good research, can afford to lose the money, and most of all, enjoy the process.

Depending upon your risk appetite, you may occasionally want to select and purchase some individual stocks or bonds.

Tip 4: Learn The Basics Of Tax-Advantage Investments

"A dollar saved is more than a dollar earned
because you don't have to pay income tax."

- Ankala Subbarao

Ankala's advice refutes Benjamin Franklin's well-known saying, "A penny saved is a penny earned" by bringing taxes into the picture. To invest on your own, you don't need to be a tax expert, but you can't ignore taxes either. Certain investments allow you to save "tax-deferred" — meaning you don't have to pay tax on the amount you invest. In traditional tax-deferred accounts, money goes into the account tax free and grows tax-free until you withdraw it. In Roth accounts, your money goes into the account after tax and also grows tax free but the added benefit is you won't have to pay taxes on withdrawals in the future. In almost all situations, you'll want to take advantage of these types of tax-deferred investments.

Tax-deferred means you don't have to pay tax on the amount you invest until you withdraw it.

In 2017, 54% of American workers participated in a retirement plan.

According to the Bureau of Labor Statistics (BLS), in 2017, 54% of American workers participated in a retirement plan. Most often, you should max out employer-sponsored tax-advantage plans first, mainly because your contributions are often matched by your employer. For example, if you contribute 5% of your pay up to a certain amount of money,

your employer may match the 5%. Unless you're going broke, you should save up to the full amount your employer matches because that is essentially free money.

Examples include Simple IRAs, 401(k)s, 403(b)s, and others. These plans have confusing names, but the bottom line is that they enable you to deduct money directly from your paycheck tax-exempt and deposit it directly into an investment within whatever options your employer's plan offers.

Each of these plans has lots of rules, regulations, and features you'll want to learn. For example, for some 401(k) plans, you can borrow money for certain purposes using your plan assets as collateral. Many of these plans offer a free financial advisor who provides you with recommendations as to which funds are probably the best fit for you based upon your age and risk profile.

In summary, here is a checklist with regards to your employer-sponsored program:

- ✓ Max out investments that are matched by your employer.
- ✓ Learn your plan's unique features and rules.
- ✓ Take advantage of your plan's free financial advisor to gain insights.
- ✓ As you age, continue to rebalance your percentages in various asset classes as necessary, keeping in mind your entire net worth.

Let's say you don't have an employer-sponsored plan or you have maxed it out totally and would like to save more for retirement.

Here is a table that shows the basics for a few common tax-advantage investments:

| NAME | 2021 CONTRIBUTION LIMIT | NOTES |
|-------------------------|--|--|
| IRA | \$6,000 under age 50 \$7,000 over age 50 | Check rules (e.g., restrictions if you already contribute to an employer-sponsored program). |
| Roth IRA | \$6,000 under age 50 \$7,000 over age 50 | Check rules (e.g., income limits). |
| 401(k) and 403(b) Plans | \$19,500 under 50 \$26,000 over 50 | Check rules for your employer's specific plan. |
| 529 College Savings | Most plans are unlimited, but be aware of IRS "gifting" rules. | Check rules (e.g., states sponsor 529 plans and each one is different). |

The devil is often in the details when it comes to taxes. First and foremost, ask your accountant for clarity before you make tax-advantaged investments. For example, in 2019, to be eligible to contribute to a Roth IRA, a married couple can't earn more than \$203,000.

Tip 5: Keep Your Assets Balanced

"Don't confuse symmetry with balance."

- Tim Robbins

Balancing assets (a.k.a., “asset allocation”) is the process of maintaining the proper amount in various types of investments based upon your propensity for risk, your goals, your investment horizon, and other factors. For example, let’s say you determine that maintaining 50% of your assets in stocks, 15% in bonds, 15% in real estate, and 20% in cash or cash equivalents is the best balance for your situation. If that’s the case, you’ll need to purchase and maintain that balance.

In the quote above, actor and writer Tim Robbins is probably referring to the fact that a good story needs balance, but it also needs artful, “asymmetrical” aspects to it. The same is true for asset allocation. You can’t make the process of balancing your assets an exact, symmetrical process because your life is fluid, artful, and ever-changing. But you still need the right mix of asset types in your portfolio.

The key to finding your ideal asset mix is balancing risk versus the growth you need in order to hit your goals.

Asset allocation is an important topic in the financial advisory world. There are books and articles everywhere on the subject. The key to finding your ideal asset mix is balancing risk versus the growth you need in order to hit your goals. There are other factors such as your age, your “needs” versus your “wants,” and how much knowledge you have about investing. (The less knowledge you have, the less risk you may want to take.)

As asset prices fluctuate — and when you make large investments such as buying a home or a car — so does your mix of assets. Therefore, over time, you’ll need to reallocate.

Here are some tips for maintaining the proper asset allocation.

- **Maintain a consolidated asset view:** If you maintain multiple accounts like many people do, then you’ll need a way to view all of your assets holistically. For example, if you have two 401(k) plans, one IRA, one taxable account, and several banking accounts, you’ll need to portion out each account’s stocks, bonds, and cash. What if a mutual fund within one of your 401(k) plans invests 65% in stocks and 35% in bonds while another invests 80% in stocks and 20% in bonds? You see the point. This may appear easy to do, but the process can be tricky and time-consuming. One solution is creating a spreadsheet with formulas yourself. Another solution is to purchase software that will do it for you, such as Quicken and Personal Capital.

You’ll need a way to view all of your assets holistically with a spreadsheet or software.

- **Review your balances quarterly or after big changes:**

Once you've decided upon what asset allocation is ideal, you'll need to review the percentages on an ongoing basis. A good way to do this is setting up a calendar reminder four times a year to compare your actual asset allocation to your goal. If your allocation is just a little bit off (e.g., plus or minus 3%), there's no need to make trades or reallocate assets. Instead, stay the course. But if you experienced a more significant change, then you may need to sell, for example, equities, and use the proceeds to purchase bonds. But remember to be careful when selling investments to make sure the corresponding capital gains taxes don't eat into your portfolio more than necessary over time. If you make a big purchase such as buying a house, you'll likely need to gradually get back to your ideal asset allocation.

Set up a calendar reminder four times a year to compare your actual asset allocation to your goal.

- **Don't allocate your assets too quickly:** Some investors try to allocate assets too quickly and therefore may suffer losses. Here is an example: Let's say you inherit \$500,000 in cash and determine your best asset allocation is 75% stocks (\$375,000), 15% bonds (\$75,000), and 10% cash (\$50,000). This asset allocation, overall, may be the correct one, but you

Some investors try to allocate assets too quickly and therefore may suffer losses.

may not want to make this allocation all at once. Why not?

Because if the stock market corrects 30% in the next few years, you would lose a lot of money. Instead, consider a more conservative approach by purchasing the \$375,000 worth of stocks over a three-year period by dollar cost averaging. Then, if the stock market goes down, you'll be making investments at a lower price and benefit in the future.

As you can see from the above tips, asset allocation is artful and ever-evolving, so your approach will never be "symmetrical" or perfect, but it should be balanced.

Tip 6: Understand
the Difference
Between
“Traditional” and
“Alternative”
Investments

Examples of traditional investments are mutual funds managed by large, well-known firms, bank deposits, large, profitable companies, publicly-traded stocks, highly-rated government and corporate bonds, and low-risk rental homes with small mortgages. These investments, generally speaking, have lower risk of losing principal especially over the long-haul.

Examples of alternative investments are ownership in a new, small business (i.e. a “startup” or a restaurant), “penny” or small company publicly-traded stocks, high-yield, lower-rated bonds, venture capital, new real estate developments, or even show horses or old cars.

Here are six suggestions when considering alternative investments versus traditional ones.

1. No matter what the seller of an alternative investment tells you, the risks associated with these investments are almost always greater than the risks associated with traditional investments.
2. There’s nothing wrong buying into alternative investments, but it’s critical to not bet the farm on them. Think carefully before investing more than 10% of your investible assets into alternative investments.
3. When it comes to alternative investments, invest in assets you already know a lot about. For example, if you’re an expert in old cars, then invest in that – not because your broker or friend is an expert and asks you to join along.
4. Do not fall for the pitch, “There’s very little risk, but this a huge return!” or “How can we lose?” That proposition does not exist.
5. Carefully weigh the risk versus return. If there is a reasonable chance you may lose your investment, then make sure you’re projected to receive an excellent return if it meets expectations.
6. Make sure you completely understand and feel good about the details of the business deal. Normally, these details are provided in an investment or an operating agreement.

Conclusion:
Keep on Learning!

We hope this guide has helped your financial journey. Remember, managing your investments is a process, not an event. Enjoy the ride! Warren Buffett has such a way with words and has been quite a savvy investor, so we might as well listen to him. Here are two additional pieces of advice from him:

“Price is what you pay. Value is what you get.”

– Warren Buffett

In this advice, Buffett is probably referring to the price you pay for a particular investment. But it applies just as well to financial advice. **Price and value are different things.** Always know what you’re paying for advice – and then compare that advice to the value you get from it. If you’re paying \$5,000 per year – or \$10,000 – or 15,000 – is the value there?

“Risk comes from not knowing what you’re doing.”

– Warren Buffett

Learn the basics. Think long-term. Don’t panic. Read what the experts have to say. Don’t invest in anything you don’t fully understand. Start small and build up. Ask knowledgeable people for tips. Try not to get overwhelmed by the financial industry’s many intricacies. (Remember, that’s what they are – intricacies.) Often times, the financial industry’s jargon is what is so confusing. Each time you read or hear a financial term you don’t know, go to Investopedia.com – a resource that explains financial terms in plain English.

We hope you’ll consider Tilly to provide you with fee-only financial advice!

- **We’re affordable** – only \$800 per year.
- **We’re virtual** – meetings are short and to-the-point, saving you precious time.
- **We’re easy** – meet with us anytime that is convenient for you, Monday through Friday.

Tilly saves you a fortune (literally)
in financial advisory fees.

[Learn more](#)

The logo for Tilly, featuring the word "tilly" in a lowercase, sans-serif font. The letter "i" is stylized with a black dot and a trail of small red dots extending upwards and to the right, suggesting a rising line graph or data trend.