HOW TO SELECT A FINANCIAL ADVISOR

One of the primary responsibilities of an investment advisor is to help you preserve and grow your savings. The truly effective ones will, among other things, help you with short-term goals, such as saving for a child’s college tuition, and long-term goals, such as retirement preparation or achieving financial independence.

There are a lot of overlapping titles and occupations within the financial sector. When looking to identify and select an individual who can help you achieve your financial objectives, one of the first hurdles involves overcoming the anxiety about who exactly does what in our industry. Confusing investment advisors with stockbrokers, insurance agents, or even with the affable salespeople at the local branch of a national Wall Street chain can prove costly and can negatively impact your progression toward achieving your goals.
A stockbroker is typically a person you might call to arrange for them to buy or sell a particular stock. Most stockbrokers don’t actually care what you buy (or order), because they typically receive a commission every time they complete a transaction for you (which means performance, accountability and the suitability of any particular purchase are often afterthoughts).
Insurance agents typically make their living by convincing you to purchase as much coverage (and the most complex policies) as possible. That’s not to say your long-time insurance agent is in any way trying to hurt you or isn’t your friend. Many insurance agents are exceptional people who just happen to view the world through a lens of risk. They are doing their part to help protect you from harm. One of the ways they do this is by insuring you against everything from alien invasions to swarms of locusts. So while it’s true that it’s better to have insurance and not need it, than to need it and not have it, and while we recommend our clients procure various types of insurance as a hedge against risk, when it comes to insurance agents and investment products, it’s a different story entirely.

Many insurance agents sell things called “annuities” which, in exchange for a lump sum, pay you a monthly amount for a specified period of time. Some annuities (depending on your individual circumstances and the interest rate you receive) are beneficial, but the ones that are often the best for the seller are the type that tie you into a long-term and inflexible commitment. Some annuities are expensive, offer poor returns, and are difficult (or impossible) to get out of should you ever change your mind or need your cash.

It’s worth noting that, in some states, licensed insurance agents can become eligible to sell annuities with as little as 4 hours of online training.
Another financial services sector individual who might not have your best interests in mind is the affable salesperson who works at the strip mall location of a big Wall Street firm or national bank. You know these chains because they have a branch on every corner.

While certainly some terrific people work for such companies, the reason they have a branch adjacent to each Starbucks is, at least in part, not because they dispense personalized advice, but because they sell cookie-cutter products (typically in the form of mutual funds) that they’ve created.

That’s right. When you invest in a mutual fund from many of the big Wall Street firms, you are usually buying a product that the mother ship has created. Certainly, some of these mutual funds could be reasonable investments, but many, though highly recommended by the Wall Street firm, have no business in your portfolio.

Often, the entire reason a particular fund is being offered is that EACH sale of that fund not only pays the salesperson a nice commission, it pays the firm an additional fee, as well. In the financial sector, that’s called “double dipping.”
When it comes to investing and retirement preparation, it’s important to note that just because someone calls his or herself a “financial planner” doesn’t guarantee that they are in any way looking out for you. An independent office with a name like Wiley E. Coyote Financial Planning is no guarantee of integrity or expertise.

The simple fact is that “financial planner” is a generic term and just about anyone can use it.

Confused yet? We’re going to help.

Most people say that, above everything else, they want honest investment and planning advice that ALWAYS looks out for their best interests. (Most people report they also want to be heard and clearly understood.) Obviously, as outlined earlier in this guide, there are several professions within the financial services sector that do not do this. Where? What? How do you find professionals who are looking out for you? It’s not that difficult, so long as you are clear about what questions you should ask to a potential advisor.

There are two industry standards that will help you achieve this clarity. While both are well-intentioned, and were implemented to serve the public, one falls a bit short merely because of a small loophole.

IS A FINANCIAL PLANNER THE ONLY WAY TO GO?
The first is called the “suitability standard.” The suitability standard is perfectly noble in that it requires advisors to only make recommendations that fit each individual investor’s needs. For instance, an advisor must never place a 95-year old client in an annuity that pays off over 30 years.

The problem is that the suitability standard, while decent for investors, DOES NOT BY ITSELF ensure that you are getting the best available advice.

Here’s a simplified example: Let’s say you explain to your advisor what you want from your investments. After doing some research, narrowed down from a list that is hundreds long, the advisor identifies 10 mutual funds that, to varying degrees, meet each of your wants and needs. While any of the 10 would cover you, for the sake of example, it ALSO just so happens to be true that 2 of those 10 investments not only pay this commissioned advisor substantially more money, but perhaps they also happen to be slightly riskier investments than the other 8. (We’ll get to the differences in advisor compensation shortly.)

Which of those 10 mutual funds do you think this type of advisor is going to most strongly recommend? The problem with the “suitability standard” is the obvious potential for a conflict of interest beneath its broadly defined umbrella. The loophole is further expanded by the fact that this conflict may not be clearly made known to you.

So the suitability standard, while well intentioned (and while we of course adhere to it as a part of our process) contains far too much gray area for our comfort and, while many firms only adhere to this rather loosely defined standard, is far from ideal.

When it comes to selecting an investment professional to work with, it’s an adherence to the “fiduciary standard” that you should insist upon.

Make absolutely certain you ask the following key questions when interviewing a prospective financial advisor:

- Are you a fiduciary? Will you put it in writing?
- What licenses and credentials do you have? What is your education?
- Are you registered with the Securities and Exchange Commission?
- Do you have any criminal complaints against you, or have you ever been suspended by the SEC or FINRA?
Who should you hire as an advisor?

Some people can manage their own investments. But even the people who have mastered some of the complexities associated with financial planning and investing, often grow weary of the grind and eventually choose an investment firm, if only to relieve the burden and enjoy life. The reason is that no one can remain totally impartial about their own financial affairs quite the way a third party professional can. Simply, you probably don’t fix your own car, you certainly wouldn’t take out your own appendix, and you probably shouldn’t manage your finances if you want to achieve financial independence, a secure retirement, and free yourself up to enjoy life to the fullest.

The monetary environment is complex. There’s confusing (and ever-evolving) tax laws, changes to Social Security (when to claim benefits, when to file and hold), busy schedules, procrastination, these are just a few of the barriers to the hands-on, attention-to-detail work involved with staying on track to achieve your financial goals. Mistakes are costly. And when it comes to money, impartiality in the form of a third party professional is important.

Know how your advisor gets paid

As detailed above, it’s probably best to avoid advisors who work solely on commission. Where commissions are involved, advice can be tainted because they have a vested interest in steering you in a particular direction. It all goes back to finding someone with a fee structure (a percentage of assets under management) that is backed by a fiduciary promise. This approach is consistent, and you know your interests are at the foundation of the advice they give.

Run a background check on your advisor

Ask any prospective advisor if they’ve ever been convicted of a crime, or if they are currently under investigation by any regulatory body. Then ask for references from a few of their other clients.

Ask about their education and credentials

While the CFP® is the gold standard for investment advisors, there are other credentials that great advisors also have. Many years of experience and a proven track record are also important.

Avoid Advisors who Promise Big Returns

If a first-meeting with an investment or planning professional includes pie-in-the-sky pronouncements of big returns due to their brilliant investment acumen, head for the nearest exit. Every investment contains risk. It’s your money, so steer clear of anyone promising a certain return.

1 The CERTIFIED FINANCIAL PLANNER™ (CFP®) designation is a professional certification mark for financial planners conferred by the Certified Financial Planner Board of Standards (CFP Board) in the United States. To receive authorization to use the designation, the candidate must meet education, examination, experience and ethics requirements.
Conclusion:

Your relationship with an investment advisor is easily one of the most important professional associations you will ever have. If they do their job, it should last a lifetime. But there are many variables. In the end, what you want is someone who is legally obligated to look out for you, listens to what you have to say, has plenty of assets under management, some respected credentials, and some great (and reliable) recommendations from clients. Follow those basic guidelines and you’ll greatly enhance, not only your odds of achieving your financial goals, but your overall enjoyment of life, as well.