"Who you gonna call?"

Two Morningstar articles address the difference between an Investment Advisor and a Financial Planner, the designations you should look for and some of the questions you should ask. The unedited versions:
http://news.morningstar.com/articlenet/article.aspx?id=819250
http://news.morningstar.com/articlenet/article.aspx?id=819893

Choosing a Financial Advisor: An Investor's Checklist

By Christine Benz | 08-03-17

Think back to the last time you bought a car. Did you buy the same car your sister owns because she likes hers? Did you shop for $16,000 Honda Fits, $85,000 Land Rovers, and everything in between? Did you head into the dealer with no knowledge of prices, fuel economy, or vehicle safety features?

Heck no, right? ... so you no doubt started the process by thinking about your needs, wants, and budget. You then homed in on two or three vehicles that fit your criteria. You probably did a little bit of homework, reading up on which cars receive the best ratings .... Only then did you steel yourself for the trip into the dealer to make the buy, praying for the shortest, most painless car purchase possible.

What's surprising is that many investors take the former tack when choosing a financial advisor, being amazingly haphazard even though, over a lifetime, their financial-advice engagement could be far more costly than a car. They begin by soliciting advice on advisors from people who may or may not know what they're talking about and who may have needs that are completely different from their own. They don't let their own needs, wants, and budget drive the process, and they often don't do much homework.

Why are investors so laissez-faire about finding financial advice?

A key reason is that the financial advisory profession is an awfully big and confusing tent. It encompasses people who are focused primarily on investments and those who construct comprehensive financial plans. Commission-based brokers can call themselves financial advisors, but so do many fee-only folks who never touch commissions.

The industry hasn't necessarily helped extinguish the flames of confusion. Despite a recent (and c'mon, totally commonsense) Department of Labor rule that would require all advisors to be fiduciaries when consulting on retirement matters--that is, be legally bound to serve their clients' interests ahead of their own--some parts of the industry have pushed back against such a standard. As noted below, the Trump Administration is once again seeking to delay the mandate. Today, the financial advisory space remains a wild west of confusing titles, designations, and compensation schemes.

The good news is that selecting an advisor who's a good fit for your needs doesn't have to be an overwrought process. A lot of guides to choosing an advisor focus on questions you should ask the *advisor*--compensation schemes, designations, and whether the advisor is a fiduciary. Those are hugely important issues, and I'll tackle that topic in a separate article. But the real first step when seeking an advisor is to think through what *you're* looking for: your goals in seeking an advisor, what sort of relationship makes sense given those goals, and how much help you expect to need on an ongoing basis, among other issues. Armed with that information, you can then seek advisors who fit your self-made description.

Here are the key questions to ask yourself.

Question 1: Are you seeking help with your whole financial life or your investment portfolio?
A key fissure among financial advisors is focus. Many financial advisors--often called investment advisors or

wealth managers--devote a lot of time and energy to managing portfolios: determining asset allocation, selecting investments, and so forth. In fact, that may be the one and only thing they will handle for you, or they may tackle nonportfolio aspects of your financial life, but do so only tangentially. As a fee-only Registered Investment Advisor, Hughes Capital Management's primary focus is portfolio management.

Another big contingent of advisors--financial planners--concern themselves with holistic financial planning: setting and quantifying financial goals, paying down debt, determining insurance needs, and investing appropriately for college and retirement, among other tasks. Financial planners know investments, too, but investment selection and portfolio monitoring aren't all they do.

Those distinctions may seem obvious to people inside the investment industry, but many consumers aren't aware of them. They might think of financial planning as interchangeable with investment management and advice. And it's true that the lines between the professions have grown blurrier in the past few years. Investment advisors are increasingly focused on providing holistic financial planning, as some consumers consider the investment-advice piece to be more or less a commodity and are seeking broader expertise. It's also true, as I discussed here, that investors sometimes think they have a "portfolio emergency" when in fact their investments aren't the main thing that ails their financial plans.

If you're seeking holistic planning advice: A financial planner is appropriate if you're seeking broad financial-planning guidance--on your investment portfolio, but other parts of your plan as well. Seek out someone who calls him/herself a financial planner and ask prospective planners if they've earned the certified financial planner or chartered financial consultant designation. Many financial planners are also fiduciaries; to be sure, ask the planner about that before hiring him/her.

If you need investment advice first and foremost: If you think your financial plan is in good shape overall but you need help selecting and overseeing your investments, an investment advisor may be the way to go. Such individuals are frequently registered investment advisors or are employed by a firm that is; these advisors and advisory firms are held to a fiduciary standard. The gold-standard designation for this type of advisor is the chartered financial analyst (which I hold), discussed here.

Question 2: Are you seeking advice on a few specific issues or do you need help with your whole plan? Do you need one-time/periodic help, or ongoing assistance?
Once you've determined whether you're looking for investment advice or financial-planning advice, the next step is to consider what specific items you need help with. Decide if you're seeking advice on a few specific issues, or problem spots, in your plan, or if you expect to need ongoing assistance. Knowing whether your needs are surgical or more encompassing can help you be an efficient consumer of advisory resources.

If you're seeking advice on just a few issues: If your needs are focused--for example, you'd like a review of the viability of your retirement assets given your anticipated spending but then you'll be set for the next five years or so--you'll want to seek an advisor who is willing to work with you on a per-project basis. Financial planners are more likely to employ hourly or per-engagement billing than are investment advisors. Hourly rates for financial planners often range from $150 to $300.

If you're seeking broad and ongoing financial help: If you expect that your advice need will be ongoing, paying a recurrent fee--say, annually--may be more cost-effective than paying for advice on an a la carte basis. Most advisors who charge in this way levy their fees as a percentage of your assets; the percentage may decrease the more assets you have under management with an advisor. Both investment advisors and financial advisors charge for services in this way; the average rate for a $1 million portfolio is 1% of assets under management, but people with larger portfolios are apt to pay less. ...

Question 5: Do you have a specific investment philosophy you'd like to see your advisor employ?
Are you a believer in the benefits that can accrue to index funds and ETFs thanks to their often-low costs and

tax efficiency? Or do you like to employ actively managed funds and/or individual stocks in the hope of beating the market? Do you want your advisor to be strategic in managing your asset allocation (i.e., long-term and hands-off), or more tactical in his or her strategy? Thinking through your investment beliefs and articulating them to a prospective advisor is a crucial step, especially if you're leaning on the advisor for ongoing investment guidance.

If you have a specific investment philosophy you'd like to see the advisor employ: If you're reading Morningstar.com, it's a good bet that you have developed a set of investment beliefs that you'd like to see embedded in your plan, even if you're delegating the specific decision-making to an advisor. Be sure to quiz any prospective advisor on his or her investment approach.

If you're open to allowing the investment advisor to ply his or her own strategy: Even if you don't have a strong view of how you'd like your assets to be managed, it's still important to ask some questions about strategy. Is the advisor clear and transparent about his or her approach? Does the advisor employ low-cost funds or more expensive ones? How much attention does the advisor pay to tax efficiency? Taking the time to understand your advisor's strategy can help you stick with the program through varying market conditions.

5 Questions to Ask a Financial Advisor

By Christine Benz | 08-06-17

Investment guru Bill Bernstein once quipped that by the time you know enough to select a high-quality financial advisor, you could probably manage your assets on your own.

Sadly, that's not all that far from the truth. As I discussed last week, the financial-advice industry features a bewildering array of titles, designations, and compensation schemes. Some advisors are fiduciaries, some aren't. And even though advisors must obtain licenses if they're selling securities, and pass tests and log work experience if they want to earn certain credentials (such as the certified financial planner designation), there aren't any minimum standards in place for calling yourself a financial advisor. You could work your whole life selling cars and no one would stop you from hanging out a shingle as a financial advisor tomorrow; you'd be competing head-to-head with advisors with years of experience and prospective clients wouldn't necessarily know the difference.

It's no wonder so many investors shortcut the process, opting for recommendations from friends and family members with limited financial backgrounds. Nor should it come as a surprise that lesser advisors who happen to be strong salespeople can rake in clients, while skilled but less slick financial professionals toil in obscurity.

People skills *are* important when it comes to getting financial help; financial matters are highly personal, so you need to have a basic comfort level with any individual you're entrusting to help you out. But you also need to conduct due diligence before signing on with an advisor. The process can be broken down into two, rather manageable, steps. The first, which I addressed last week, involves taking stock of your needs in the realm of advice consumption. The second step, which I'll focus on today, is to take what you just learned about your own needs and goals to identify an advisor who can help you meet them.

Here are the key questions to ask of prospective advisors.

1. Are you primarily a financial planner or an investment advisor?
This is one of the first forks in the road that investors will encounter when surveying the universe of financial advisors: There are wealth managers/investment advisors, and there are financial planners.

The former type of advisor has a narrower purview--investments--than do financial planners, who consider all major aspects of a financial plan, not just investments: insurance, estate planning, and household budgeting, to name a few. However, it's worth noting that the best investment advisors think holistically about their clients' plans, while many financial planners possess topnotch investing acumen. So there's not necessarily a bright line.

If you're seeking a financial planner: Ask prospective planners about their areas of special expertise, and the demographic they typically serve. If you've identified specific areas you need to work on--for example, figuring out how your small-business ownership impacts the rest of your personal financial plan--ask the planner if he's had experience with situations like yours. Also look for someone who has earned the certified financial planner or chartered financial consultant designation, discussed below.

If you're seeking an investment advisor: Ask about investment strategy: Does it jibe with your own philosophy? Does the advisor use basic portfolio building blocks like low-cost mutual funds, or dabble in more arcane investments like futures and options? Is the strategy readily understandable? (If not, ask every question you can think of until it is. If the advisor gets exasperated, you're not a match.) The gold-standard designation for this type of advisor is the chartered financial analyst (in which case CFA will appear after the Advisor's name).

Softer, but no less important, does the advisor approach his or her job with a healthy dose of humility? You can get at that by asking about what he or she expects a balanced portfolio to return over the next decade. Any advisor who's promising portfolio returns higher than the midsingle-digits over the next decade isn't being realistic and/or may be taking excessive risks.

2. Are you a fiduciary?
The Department of Labor's "fiduciary rule" has been one hot topic among financial advisors over the past few years. Simply put, the rule would require all financial advisors to put their clients' interests ahead of their own when consulting on retirement portfolios. Some portions of the rule went into effect earlier this year, but it has been contentious.

The good news is that many financial advisors already adhere to a fiduciary standard. Investment advisors who are registered investment advisors--or work for firms organized as registered investment advisors--are already fiduciaries. Certified financial planners are required to act as fiduciaries when offering planning advice, but they may not be when they're selling securities. (I know, too confusing.) Your job is to ask the question outright: Are you a fiduciary, and will you be one in every context in which you'll serve me?

That's not to suggest that financial professionals who aren't fiduciaries are automatically unethical hacks, by the way; many non-fiduciaries uphold high ethical standards and treat clients with every bit as much care as their fiduciary counterparts. But investors who work with a fiduciary have a higher level of legal protections than if they work with an advisor who's held to the lower "suitability standard." The latter type of advisors need to be able to defend their recommendations as being appropriate/suitable for you, versus fiduciaries, who are legally obligated to recommend the "best" products for you given your situation.

3. How do you charge for your services?
Advisor compensation can get messy. One of the first questions to ask is whether the advisor is fee-only, fee-based, or commission-based. Fee-only means that the advisor is compensated by charging fees for various services and is never compensated with commissions. Commission-based advisors obviously accept commissions for recommending products. Fee-based advisors may charge primarily fees for services they provide, but may also accept commissions.

As with the fiduciary discussion above, advisors who accept commissions shouldn't automatically be marked with a skull and crossbones. But receiving commissions for products can introduce conflicts of interest, incentivizing advisors to recommend products that aren't necessarily in clients' best interests. The fee-only model is cleaner. And while the commission model is often touted as a way for investors with smaller portfolios to gain investment advice, that's a straw-man argument, as I discussed in this video. ...

Percent of Your Assets: Many investment advisors charge in this fashion (often called the assets under management model), taking a percentage of the client's assets under management on an ongoing basis. The average rate is 1% for a $1 million portfolio, though clients with larger portfolios will generally pay a lower percentage. (After all, managing a $2 million portfolio isn't necessarily double the work of a $1 million portfolio.) Such fees are usually on top of whatever the investment fees are; for example, if an advisor charges 1% and puts the client in a portfolio with average fees of 0.35%, the client's fees are 1.35%. Advisors who employ the AUM model often have minimum portfolio thresholds; $1 million is a common level. HCM's is currently $100,000.00.

Best for: The AUM model is best for delegators who expect to need a fair amount of ongoing help and would also like to be able to be able to contact their advisors with questions or concerns on a regular basis. These consultations are baked into the ongoing fees you're paying, so you should be the type to take advantage of them. ...

4. What designations/credentials do you have?
In addition to getting clear on how you're compensating the advisor, it's also worth asking about designations the person has earned. Don't be blinded by a long list of letters after the advisor's name; some designations, such as the following, carry more heft and have heavier requirements than others. (Note: There are several other worthy designations for advisors, such as chartered life underwriter [CLU], but they're not as broadly applicable as the following.)

If you're seeking a financial planner, look for the following:

Certified Financial Planner (CFP): A certified financial planner is a financial planning expert accredited by the Certified Financial Planner Board of Standards. In order to use the CFP designation, planners must complete an educational program, pass a comprehensive exam, and log extensive financial planning-related work experience.

Chartered Financial Consultant (ChFC): Much like the better-known CFP, this is a broad financial-planning designation. Chartered financial consultants must complete an educational program and a series of exams, while also logging related work experience.

If you're seeking investment advice, first and foremost, look for the following:

Chartered Financial Analyst (CFA): Individuals with this designation qualify as financial experts accredited by the CFA Institute. In order to use the CFA designation, advisors must log substantial work experience involving investment decision-making and take courses on subjects such as economics; financial reporting and analysis; ethical standards; equity and fixed-income investments; and portfolio management. They also must pass a series of 3 rigorous exams requiring substantial study time.

5. What's your backup plan?
Even if your advisor is young, it's still worth asking about backup planning. Who would step in and offer assistance if the advisor could not do so for a period of time, due to death, illness, or even a long vacation? Especially if you're hiring an advisor on an AUM or retainer basis--but even if you're not--there should be individuals in place to serve as backups if your primary advisor isn't available.

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From August 7th's The Finance 202:

The Labor Department is seeking to delay the compliance deadline of the fiduciary rule by 18 months as it seeks to rework the Obama-era mandate. That would push the effective date for the rule to July 1, 2019. The Wall Street Journal's Lisa Beilfuss reports: The fiduciary rule 'is likely here to stay, but its impact could be significantly reduced over the next few years if exemptions from the rule are significantly expanded,' said Jamie Hopkins, a professor at the American College of Financial Services... The first phase of the rule, requiring financial-advice providers to act in retirement savers' best interest, took effect June 9. The request for a delay would give agency officials more time to conduct their economic-impact review and give industry players more time to weigh in." We doubt that "more time" for "industry players" to act in the best interest of their clients is in their clients' best interest.

Our thoughts

"If there's something weird
And it don't look good
Who you gonna call?"

Knowing who to call and what to ask when you call matters.