

Selecting a Financial Advisor

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- ▶ Selecting a financial advisor who is both ethical and competent may seem like a daunting task, especially with the recent convictions of Ponzi scheme operators Bernie Madoff and Allen Stanford.
- ▶ However, you can protect yourself by following this outline of important factors to consider in selecting a financial advisor.

Financial advisors have long played an integral role in providing guidance to individuals and families in the areas of investments, retirement planning, education funding, and similar financial planning needs. You may benefit from the counsel of a financial advisor, but what factors should you consider when evaluating a financial advisor?

Factors to Consider

Honesty is the first critical hurdle that an advisor must clear.

*** Integrity/Trust:** An advisor's integrity is essential in order to have faith in their recommendations. An effective advisory relationship cannot exist without integrity and trust. Use your initial interactions with a financial advisor to determine their level of integrity. I had one prospect tell me part way through our first consultation that I had passed her "smell test." While this may be a gut response, it is also an accurate reflection of what you are attempting to determine: Is this person a crook or are they honest?

*** Compliance:** You may investigate the background of an advisor and their firm via one of two resources on the Internet. For a registered investment advisor (RIA) or their firm, visit www.adviserinfo.sec.gov, whereas if an advisor operates as a broker (more on this later), you will want to access www.finra.org/brokercheck. These sites list any infractions that are known to regulators and can provide you with insight as to the compliance record of a firm and its principals.

Once you have evaluated an advisor's integrity, you still must determine whether they are competent.

*** Credentials:** Dozens of credentials exist in the financial advisory field, but most should carry little weight with individuals looking to hire a financial advisor. The most relevant designations to a financial advisory practice are Chartered Financial Analyst (CFA®), Certified Financial Planner (CFP®), Certified Public Accountant/Personal Financial Specialist (CPA/PFS®), and Chartered Financial

Consultant (ChFC®). In addition to these credentials, advisors may also hold one or more securities licenses, though these are more prevalent among brokers. Note that these credentials and securities licenses provide only a foundation of knowledge in the financial advisory field and are not a substitute for experience.

*** Experience:** Another differentiating factor between financial advisors is their depth and breadth of relevant experience. Scrutinize their background. Many financial advisors have not advised clients through several market cycles because they are either too inexperienced or were employed in an unrelated field earlier in their career.

Once you believe you have found an honest and competent person to dispense financial advice to you, consider the business model that they operate within.

*** RIA versus Broker:** Under current law, an RIA has a legal, fiduciary duty to act in a client's best interests. A broker, on the other hand, is held to a lower standard, one of suitability. As such, an advisor who is a broker is required to recommend products that are appropriate for their client, but may not be in the client's best interests.

*** Compensation:** A financial advisor's compensation usually follows one of three models: fee-only, fee-based, or commission-based. Fee-only attempts to align an advisor's interests with a client's by charging based on the amount of investment assets overseen or on an hourly or fixed fee basis. A fee-only practice tends to be more advice oriented, whereas a commission-based practice tends to be more product driven with the advisor receiving commissions based on selling investments or financial products. Fee-based is a compensation arrangement that can include fees or commissions.