

How to Find and Select a Good Financial Planner and Wealth Manager.

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The
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Individuals and families who are looking for a financial advisor must explore the investment jungle alone. It is not easy. This material is designed to give you a "travel guide."



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This paper is written for the majority of investors who struggle with investing by themselves without help. Should you go it alone or use an advisor? *This is the threshold question.*

The authors confess: we think you should use an advisor—but then, we are in the advice business. You expected us to say that, didn't you? Yes, we have our biases, but that doesn't mean our answer is not true. We think everyone should use an advisor.

In this paper, we'll tell you why that's a good idea. We'll also tell you how to go about looking for a good advisor and how to recognize one when you see him or her.

EXPERTS DO BETTER THAN AMATEURS

You can't invest yourself as well as you could if you had an expert advisor. Here's why.

Like any other occupation, to be an expert investor, you have to have appropriate education, knowledge, skills and abilities, and—most of all, experience. To be good, you have to work at it full time.

Would you expect someone to be an expert lawyer or doctor if he had not gone to law school or medical school? Even if he had the education, would you think he could be an expert practitioner if he only worked at it on weekends? The same can be said of almost every occupation.

We live in a world economy characterized by the specialization of labor—no one person knows how to make a pencil from start to finish. Almost every

occupational pursuit is so specialized only those educated and experienced, and who work at it full-time are really good at it. This is certainly true of the investing business. It is highly segmented into specialties.

Furthermore, investing and portfolio management changes and evolves just like every other business in a modern, market economy. You have to run at top speed just to keep up with developments. It draws some of the brightest minds. It offers handsome rewards for success. If you work at something else, you haven't got a chance to compete favorably with professional investment managers. Those who dabble at an occupation perhaps can become informed amateurs but will stay amateurs nevertheless.

SELF DECEPTION

It is amazing how many lay investors delude themselves into thinking investing is unlike every other occupation—it can be mastered by reading a few books, magazines and by watching some weekly talk show on television.

The same person who flies to the pediatrician when his kid gets the sniffles—who would react with horror if you suggested he become a physician to his family by

reading a few medical books and taking a course on first aid—this same person can delude himself into thinking investing is easy. They're thinking: "Sort of like learning to knit, isn't it?"

Why does this self-deception take place? Because, for some people, investing offers "rewards" more important to them than investing success. Here are a couple of so-called "rewards."

Reward 1: The Excitement of Gambling

Investing is full of uncertainty. People remember with excitement when their guesses about an investment turn out to be right. These same folks mentally suppress the memory when they turn out to be wrong. Waiting for the results is like throwing dice and seeing whether they come up with a seven or with snake eyes. Gambling is fun! If it weren't, Las Vegas and Atlantic City would be ghost towns. However, almost no one admits to the appeal of gambling in investing. They know this is not cool. By allowing themselves to continue to

gamble, these sorts of folks confuse expertise with luck. Yet, if you met someone who flipped a coin and got five heads in a row, would you conclude he is an "expert" coin flipper?

The gambling element in investing is a powerful drug. It has seduced many into using their investments as a source of entertainment. When financial catastrophe comes, the memory of the entertainment is little consolation, however!

Reward 2: Keeping Busy Instead Of Getting A Life

We have seen many people who, when retired, have turned to investing as a way to "have something to do." They fill their days reading personal finance magazines, watching investment shows on television and fiddling with the bookkeeping and administration of their investments.

One client came to us because the husband—a retired mathematician—was doing all the investing himself and was getting poor results, jeopardizing their retirement.

His wife, who hated investing, dragged him into our office. When they arrived, he carried a good-sized box full of paper. He kept meticulous track of every penny. He had spreadsheets galore. He had dozens of investment accounts, far more than needed.

When we asked why, his wife blurted, "Because the more accounts he has, the more paper he has to fiddle with!" He had seven brokerage accounts. Seven?! We asked why? Again his wife blurted, "Because he loves to schmooze with brokers. He spreads the money around so he will not overburden any one broker with telephone calls."

He and his wife became clients. They now have one investment custodial account, a well-designed and implemented portfolio and minimal administration. The husband is now active with church and volunteer work he finds very fulfilling. He spends more time with his wife. When we meet, the wife talks more about how she reclaimed a meaningful life with her husband than about investing.

HOW DO ADVISORS ADD VALUE?

If advisors claim to "beat the market," the answer we give is—it's statistically possible, but very, very unlikely. If you are naive enough to think that's what an advisor's role is, you won't get a good advisor. You'll just get one pandering to your fantasy!

On the other hand, if the advisor acts as a skillful guide and counselor through the investment jungle, then most certainly he or she will add value—lots of it. That's because the most mistakes investors make do not

occur in the construction phase of investing (although it's possible to make big mistakes there too.)

The biggest problem investors have is setting objectives properly, obtaining a portfolio design best achieving those objectives, constructing the investment house at a reasonable cost and maintaining the house properly. A good advisor is worth his or her weight in gold if he or she helps you solve these problems.

HOW TO FIND AN ADVISOR: A PLAN OF ATTACK

Let's say it right at the beginning—it's not easy to find a good advisor. It takes some work. However, there are some sensible ways to go about it. Just as we have said being a wise investor requires you know something about the investment business, finding an appropriate advisor requires you know something about the advice business. We will address the following topics:

- There are many players offering “advice.” You have to “know the territory.”

- The Commission Conflict
- Practicality: theory aside, can you afford an advisor?
- Discernment: How can you tell the true advisors from those who merely claim to be one?
- What are the “absolutes” and “nice to haves” in the advisory relationship?
- How to search for a good advisor: What should you expect?

KNOW THE TERRITORY

The first requirement is to know the territory before you begin your travels. For example, most people know the differences among physicians. They don't expect their family doctor to know heart surgery. They know the territory.

However, the average investment layman can't tell the difference between a broker, a money manager and a wealth manager if their life depended on it. And why should they? It's not their game. Investing is unfamiliar territory. You shouldn't go exploring without a map. You should reconnoiter the field.

It will help to keep in mind the “investing is like building a house” metaphor. Each player in the territory can be mapped into the following categories:

- Architects/general contractors responsible for planning and designing your investment house, and then picking and managing specialty subcontractors. (Wealth managers, asset managers, financial planners.)
- Subcontractors responsible for specialized construction tasks. (Money managers, mutual funds.)
- Purchase agents who specialize in buying building materials for subcontractors. (Brokers.)

Let's take a little tour of the advisory territory.

Wealth Managers

A wealth manager acts as an architect/general contractor and provides the planning and design functions of investing. They select and supervise the

subcontractors—they maintain the investment house.

Before wealth managers arrived on the scene, investors had to do this job themselves and had to deal directly with the subcontractors and purchase agents—mutual funds and brokers. For small investors, some years ago the investment industry recognized the “general contractor” service was “missing.” There was no efficient way to provide the services except to very large investors.

The large institutions paid for general contractors—they were called “consultants.” These institutional consultants performed exactly the wealth management services described above. Unfortunately for the average investor, these consultants cost tens of thousands of dollars annually. For very large funds, annual fees of over one million dollars are not unusual. Providing these services to the small, retail investor was impossible.

The revolution in securities regulations, computer technology and custodial services since the mid-1980s changed all this. The revolution created a new type of advisor—a “wealth manager” for the retail investor.

The wealth manager is sometimes hard to recognize because of confusion with vocabulary and terminology. They are generally found using the labels: “asset managers”, “financial planners” and “wealth managers.” You have to investigate carefully to make sure these folks are not also serving as a subcontractor or purchasing agent (a money manager or broker.)

Investment Managers or Money Managers

The money manager or investment manager is a subcontractor used to build the investment house. Money managers select individual stocks or bonds for a portfolio. The business has become highly specialized. Mutual fund managers inform the public of their expertise, investment philosophy and targets. Managers usually confine themselves to a very specific room in the investment house: a specific asset class or sector, such as large-cap, domestic stock, transportation sector or intermediate-term international bonds.

Be aware: the money manager cannot reasonably fill the role of architect and general contractor. It is up to someone else to decide whether the investment house needs the money manager's specialty room. Don't ask the money managers. The wealth manager is responsible for picking the money manager.

Stock Brokers

Brokers buy and sell stock and bonds. Many investors mistake them for advisors or more precisely, money managers. They are not. Unlike mutual fund managers, brokers have no audited track record and do not report on performance.

Naively, the same people who would not choose a "public" manager (a mutual fund) without knowing something about its investment performance will, with what can only be called blind faith, let a broker pick stocks and bonds for them.

Stockbrokers are salesmen, not advisors or money managers. In most cases they desperately try to hide that fact from individual investors (institutional investors know better.) Tell a person you are a broker to someone at a cocktail party and you will almost always see that person make a hasty retreat. It's almost as bad as telling someone you are a used-car salesperson. Even though we need salespeople from time to time, they definitely should not be designing and building your investment house!

Many stockbrokers are very smart. They know the consequences of telling the truth. Thus, many brokers now call themselves "financial advisors, or financial

consultants"—anything but "brokers!" Similarly, insurance salespeople often call themselves "estate planners" or "business succession planners."

Nevertheless, regardless of the title, they are what they are—salespeople. Don't let them fool you. Brokers can have enormous conflicts of interest with investors depending on the nature of the relationship.

Lay investors shouldn't go near a retail stockbroker for advice or to use them as money managers. Better to put your money under the mattress.

Having slammed brokers here, joining great throngs deservedly slamming them elsewhere, this needs to be said: a good broker is worth his or her weight in gold, as is any salesperson who knows his products. Buying and selling is a very necessary pursuit in modern capital markets. The money managers use brokers as purchasing agents to acquire the stocks and bonds for their portfolios. The money manager needs excellent brokers.

The problem comes when the naive lay investor confuses the brokerage function with the general contractor function (wealth managers, financial planners) or the subcontractor function (money managers or mutual funds). It comes when the brokers misrepresent themselves as an objective advisor rather than the non-objective salespeople they are. It usually comes into play when the investor is looking for short-term "action" and is "excited" by investing. Prudent investing should not create excitement.

Financial Planners

Many financial planners offer wealth management services, helping people solve their total investment problems. There are two types of financial planners; those compensated by commissions and those compensated by fees. Those compensated by fees are "advisors." Those compensated by commissions are "brokers," because their compensation comes from product sales. Some use a combination of the two methods—it's difficult to say what they are.

The zeitgeist of the financial planning business is somewhat different than the traditional brokerage industry. The relentless pressure of product sales is somewhat mitigated. Many of those committed to

financial planning earnestly try to give unbiased advice. But, the commission conflict of interest ultimately undermines those earnest attempts. The authors came to this irrefutable conclusion almost two decades ago and switched from selling products to advice giving.

Bank Trust Departments

Bank sources of investment services range from ridiculously poor to very good. The private banking services rendered to very high net worth investors rank among the best. The services rendered to the more modest accounts are not satisfactory from an advisory standpoint.

The trust department offers the advantage of being “fee-only,” and not receiving commissions... maybe. Most regional and national banks use proprietary mutual funds and other products for their customers from which they earn larger commissions. Those that use proprietary products often limit your choices. Ouch!

Banks also do not normally report on performance. Over the years, clients have brought us dozens and dozens of bank investment statements. We rarely see a

performance report. That’s right, rarely! The reports are voluminous accountings of the movement of every penny, but not a word about performance. These bulky reports are not worth the paper they’re printed on, literally.

You might recognize the territory—banks act more like money managers than advisors. They try to fulfill both roles, but without performance reporting, they don’t fill the advisor role at all. If you owned a racecar, wouldn’t you want to know how fast it went during the race?

More important is the issue of portfolio design. Banks have traditionally used only a few asset classes. A two or three room investment house will not suit the needs of the typical investor. Some banks even select individual securities, acting like the subcontractor. In reality, this limits diversification and increases investment risk.

How do banks get to do this? They convey an image of “safety.” It’s true, no one is likely to steal the money. But at what price in reduction of return through higher fees, mediocre performance or increased risk? Fortunately, the banking industry is evolving too. These characterizations may require amendment in the future. Banks tend to think of you as a customer, not a client. We’ll see if that characterization changes going forward, but we doubt it.

THE COMMISSION CONFLICT

The question for you is this: do you want to do business with someone who must daily confront the commission conflict of interest, hoping the conflict is resolved in your favor?

Think of it this way. Most people have a lot of respect for their physicians. However, do you think it would be a good idea for physicians to own pharmacies? Where would their interest lie, and how would that impact writing prescriptions?

We recommend you do business only with “fee-only” advisors. This advice will ruffle the feathers of many. We are sorry. We are not suggesting every commission-compensated advisor will yield to the conflicts of interest. We are just suggesting it would be more prudent for you to insist on a business relationship where there are no commission conflicts for your advisor to face.

We must hastily add working with a fee-only advisor

does not resolve all conflicts, just the very important commission conflict. Suppose you ask your fee-only advisor whether you should withdraw some of your funds under his management and pay off your mortgage? You had better believe your advisor would face a conflict. Saying “yes” lowers his or her revenue because their fees (based on the size of your investment account) are reduced.

All advisors have some conflicts. If you ask a surgeon whether you should have an operation, he faces a conflict. If you ask a lawyer whether you should hire him to sue someone, she faces a conflict. Conflicts are unavoidable; they can only be managed.

That being said, the commission conflict is so deleterious to your financial health it should be first on the list of conflicts to be avoided. Why tempt fate?

PRACTICALITY

It is not practical for everyone to use an investment advisor. There is the matter of economies of scale. Advisors performing the wealth manager function (architect/general contractor) typically charge one percent annually for their services—some a little more or less.

Most advisors have minimum account sizes. It varies, but a \$1,000,000 minimum is not uncommon. The better the advisor is, the higher their minimums tend to be. That's because advisors, like everyone else, have only so

much time and resources. The resources and time required are generally proportional to the number of clients served, not to the amount of money served. This drives advisors to favor account sizes where they can create the most value.

However, there are no hard and fast rules. It is possible, with a diligent search, to find wealth managers who accept small accounts, or who charge by the hour to give advice. These folks make up a very small percent of fee-only wealth managers.

HOW CAN YOU TELL THE TRUE ADVISORS FROM THOSE WHO MERELY CLAIM TO BE ONE?

Actually, this part is easier than you might think. First, look at the advisors professional credentials and background. This information should be readily available on their website, and can be verified at the licensing and certification agencies responsible for the certification.

For starters, your advisor should be a Certified Financial Planner (CFP™). This is the minimum requirement for education, experience and ethical behavior for wealth managers today. You can check the validity of the designation at the Certified Financial Planner Board of Standards website: www.cfp.net.

There are other titles out there, supported mostly by brokerage houses or small schools where you can get some sort of accreditation in a week or two. Most aren't worth the paper they're printed on for you. To become a CFP

practitioner, you must take course work lasting about a year or more, pass a multi-part national challenge exam, and fulfill a three-year practice requirement working for a firm with active CFP certificants doing planning. Not quick, not easy, and definitely not out of a cereal box!

Most top planners also have a graduate degree in a related field such as business, financial planning, law, tax, accounting, or finance, and may have additional certifications such as Certified Public Accountant (CPA), Certified Financial Analyst (CFA), Enrolled Agent (EA), Chartered Financial Consultant (ChFC) or Professional Financial Specialist (PFS).

Having said all this, certification by itself is not sufficient to determine a good fit, but if the advisor *doesn't have at least a CFP designation, we strongly recommend you move on to someone who does.*

WHAT ARE THE "ABSOLUTES" AND "NICE TO HAVES" IN THE ADVISORY RELATIONSHIP?

One should never use the word "absolute" with regard to financial matters unless it really is absolutely critical, and there is one critically important issue: *working with a firm and staff who are investment fiduciaries.*

Investment Fiduciary

You may have heard the term "fiduciary" as it relates to investment services. In fact, it's one of the hottest new buzz words in the investment industry. Even though

many have heard the term, few can actually define it. Not surprisingly, most investment professionals don't understand the role and responsibilities of a "fiduciary."

The importance of fiduciary responsibility has come into the spotlight in recent years because of the rise of corporate malfeasance. The public and regulators reeled from the Enron and WorldCom debacles—the two largest cases of corporate fraud in history. Unethical, illegal, and misleading practices by large brokerage firms, banks, and mutual fund companies have been prevalent. Prominent investment firms paid multi-million dollar fines to settle charges of unethical trading, sales and other questionable practices. With unsettling regularity, CEO's and executives of major corporations—including those of prominent investment firms—are tried and convicted for various illegal activities hurting shareholders and investors.

This creates a difficult situation for you. How do you know who to trust? What is the real definition of a fiduciary, and how do you recognize a fiduciary when you see one? Stated another way, how can you be sure the firm you are dealing with is consistently and properly fulfilling their duties to your benefit?

In practical terms, a fiduciary relationship represents the highest standard of care imposed at either equity or law. A fiduciary owes a duty of loyalty to whomever services are provided and is expected to be above reproach in carrying out their duties. They must not put their personal interests before their clients, and they may not profit from their position as a fiduciary without the consent of the person to whom they have pledged their fiduciary duties.

Chart One

| Differences Between Fiduciary and Non-Fiduciary Investment Providers | | |
|--|---|--|
| | Fiduciary Advisors | Non-Fiduciary Investment Providers |
| The Players: | Professional Fiduciary Advisors | Bank Sales Reps (Brokerage), Wirehouse and Independent Brokers, and Insurance Agents |
| Regulatory: | SEC Registered Investment Advisor (RIA) (If < \$25 million, RIAs are state regulated) | Primarily Self-Regulated by NASD |
| Fiduciary: | Acknowledged Fiduciary Status (Statutory) | Generally Limited or No Fiduciary Responsibility |
| Services: | Ongoing Comprehensive Financial Advice | Transactional: Sell Securities, Investments, and Insurance Products |
| Standards: | "Fiduciary" Standard | Must Only Make "Suitable" Recommendations (unless discretionary authority assumed) |
| Transparency: | Provide Full Disclosure via ADV | Minimal Disclosure Requirements |
| Compensation: | Typically Fee-Only for Investment Management | Commissions, 12(b)-1 and Transaction Fees |
| Competitive Advantage: | May Provide Objective Integrative Wealth Management | Often Very Skilled at Developing Relationships and Selling Products |
| Discretion: | Typically Assumes Discretionary Authority | Transaction-based; Typically No Discretion |
| Functional Role: | Planners, Advisors, Consultants, and Managers | Salespeople |

The U.S. Securities and Exchange Commission's Office of Compliance Inspections and Examinations further identifies five responsibilities of fiduciaries:¹

1. Put clients' interests first;
2. Act with utmost good faith;
3. Provide full and fair disclosure of all material facts;
4. Not mislead clients; and
5. Expose all conflicts of interests to clients.

Ok, now you know what fiduciaries look like and how they must act. But, how do you know someone is acting as a fiduciary? Fortunately, there is an international certification board for investment advisors (and other professionals such as investment stewards and investment managers) called the Center for Fiduciary Excellence (CEFEX). Located in Toronto, Canada CEFEX is the international fiduciary standards organization organized by sponsoring agencies from around the world, including the United States. You can check to see if the advisory firm you are talking with has met their exceedingly high standards at www.cefex.org. This independent audit and certification is the only independent assurance available today that the advisor is adhering to the best fiduciary practices. If they are CEFEX certified, they are professional fiduciaries, period.

Nice-to-Haves

Next are “nice-to-haves” in the relationship between the firm, its professionals and you. The first is areas of specialization and experience. If you are a senior executive with, say, stock options, you will want to work with a firm having experience with stock option issues, such as taxation, regulatory and corporate restrictions, timing, and so forth.

The same is true if you have suddenly become responsible for a large amount of wealth from inheritance, death of a spouse, sale of a business or appointment as a trustee. You'll want a firm well versed in the special issues you'll face.

The second is firm capacity and “depth on the bench.” You'll want to make sure there are sufficient professionals available to work with you in the future. Just as you want to diversify your investments, when looking for a long-term engagement, you don't want to put all your “relationship eggs” in a basket working with a solo practitioner.

Finally, a sense of comfort and confidence in your advisor and team. This is the most subjective, and the hardest to define for people. In order for this to happen, you should talk with more than one advisor in order to compare and contrast their points of view and empathy.

In the following section, we'll discuss the things to look for when selecting your advisor.

HOW TO SEARCH FOR A GOOD ADVISOR: WHAT SHOULD YOU EXPECT?

There is considerable variation in how advisors work with clients. However, we think there are important functions and processes that define high quality services. All of these steps are not absolutely necessary, but the more offered, the better the results for you. For a “full service” advisor, who practices financial planning and advises on more than just investing, the list below is mandatory. Wealth managers will also want this information and will go through this process.

Don't Rush

Planning the investment house takes time. A good advisor will not want to rush the job. Oddly, clients are the ones who often want to go fast. They are usually holders of the conventional wisdom that short-term results matter. A good advisor will try to slow these folks down. Another reason to go slow is because you will be exposed to new information and concepts. You can absorb it only so fast.

¹Fiduciary Duty: Return to First Principles,” by Lori A. Richards, Director, Office of Compliance Inspections and Examinations, U.S. Securities and Exchange Commission., <http://www.sec.gov/news/speech/spch022706lat.htm>

Another reason to slow down is some people come into money because of very traumatic circumstances. They are the beneficiaries of life insurance on their spouse or they receive an inheritance from their parent. It takes a while to recover. Widows and widowers are especially vulnerable during this period. They often think they are being irresponsible if they don't "invest" their money quickly. We tell them to stick the funds in a money market fund and relax. There is no great hurry.

Getting To Know You

Almost everything about you bears on the design of your investment house. The best advisors will spend quite a bit of time getting to know you. They will ask you for tons of information. They will want to know all about your family including children and grandchildren. They will want to construct a complete financial profile of you. This means not just assets and liabilities, but rather a complete financial statement.

For example, asking questions like: What are your sources of non-investment income: retirement annuities, social security, trusts, contracts, deferred compensation and so forth?

Do you have any life insurance? How much, what kind and who are the beneficiaries? How long will you continue to pay the premiums?

Have you done your estate planning? Can I review all your estate documents?

What is your tax status? Can I review the last two year's tax returns?

Do you have trouble saving or are you a miser?

What are your attitudes toward risk and return? (this usually involves a detailed questionnaire)

What has been your previous investment experience? Do you get sick-to-your-stomach if the Dow-Jones Industrials falls 10%?

And this is just for starters.

Beware of advisors who don't ask for this type of information. They will not do the best job of designing and building your investment house.

Goals and Objectives

A good advisor will grill you on this topic. What are your priorities if you can't accomplish all of them? Sometimes individual spouses have different priorities. The advisor will help sort them out. If the advisor doesn't emphasize your goals and objectives, you may run the risk of working with a firm that thinks everybody is the same, or who tries to fit everyone into a "one-size-fits-all" philosophy. That's not good.

Investment Tutorial

Clients show up at advisors' offices with a wide range of conventional investment wisdom, inherited from their forebears and gleaned from the personal finance media. Some of it is wise, but much of it is poppycock. It's not your fault; you have lots of company. A good advisor will want to spend some time helping you throw conventional but dangerous wisdom overboard.

Another reason for some tutorial conversations is to make doubly sure you will not have expectations the advisor cannot fulfill. Remember the building the house analogy? Some house designs just can't be built. Advisors approach this task in all sorts of ways. Some give formal tutorials. Some sprinkle it in conversations as you go along. Some give formal seminars to groups of clients at regular intervals.

Design before You Build

Blueprints. We hope you will insist your investment house be designed before it is built. A good advisor will show you his or her recommended layout of the rooms. That means the asset classes, their number and their size.

The blueprint will be a pie chart or list with this information. A modern portfolio may have a dozen "rooms." If instead, the advisor first shows you a list of subcontractors or construction materials (fund managers or stocks and bonds) he or she has the cart before the horse. Beware.

Design History. The best advisors will show you what it would have meant for you to stand in the shoes of the proposed design—the history of its performance. By looking at year-by-year past performance, you can really get a good sense of what it would have been like to live in the investment house.

Did the asset class with the best return for each year jump around? Each asset class will have its day. If one is always the best, it probably means there are not enough rooms in your investment house. Technically speaking, the portfolio is not diversified enough. The advisor should explain the role of each room in the house.

Alternative Designs. You should also be shown some alternative designs. The advisor's recommendations may be a good starting point for discussion, but you should know the alternatives. The advisor is not inviting you to second-guess him. It's just the risk-reward tradeoff is a uniquely personal decision.

Although the advisor will certainly know a lot more about investing than you do, a good advisor doesn't think he or she is God. He or she will suggest a road for you to travel. Remember, you can walk on the left or right side—not just down the middle—and you will still stay on the road. You have to take some responsibility for results too.

Construction

After you settle on the design of the investment house, you have to build it. The advisor will show you his proposed list of subcontractors. You will, by now have had to settle on your resolution of the two big investment philosophical questions. Do active managers add value? If the answer is no, then the subcontractors will be asset-class funds. All you have to know is that the subcontractor captured the performance of the asset class.

The most important consideration is costs. Asset class funds should be one-half or less than their active-management counterparts.

To the extent the manager selection philosophy allows active managers, a brief description of the salient characteristics of these funds should be given. Don't

expect the advisor to give you a fat research report on each fund. Wealth managers are in the advising business, not in the publishing business. Does your doctor give you a research report each time he or she gives you a prescription for a drug?

Custodian

Beware of an advisor who does not use a custodian. If it is because he uses only one or two mutual fund families, you have limited your choices of subcontractors. If you wanted a new car, would you want to be able to select only Saturn or Volvo? If you are doing all this on your own and your funds are small that may be OK, but not for substantial portfolios.

We recommend investors use strong, independent custodians. Have the advisor explain the transaction costs and the mechanics of how you use the custodian. Advisors usually can arrange for you to pay wholesale rates for the custodian services, well below the rates retail investor pay, even at discount brokers.

Maintenance Discretion

To what extent will you give discretion to your advisor to keep your investment house well maintained? We believe it is OK to give the advisor discretion over the asset classes that make up the house design; what subcontractors to use; and rebalancing the portfolio to keep the rooms of the investment house the proper size. However, never give advisors the discretion to change your basic risk-reward decisions. You live in the house, not him. A good advisor will communicate his decisions before or after the fact, but you'll never be left in the dark.

Performance Reporting

What to Report. This is a touchy subject among advisors. We used to give qualitative reports to clients. We would simply say the house was doing "well" or "poorly." The reason we were not more precise was not that we didn't care. Rather, the tools to precisely measure

portfolio performance were not available at an acceptable cost. However, this has changed in recent years.

You should expect your advisor to tell you exactly (to the first decimal point) how your portfolio did in the particular period under examination. But, if all you know is the return of your portfolio, we would say you only got half the answer.

Think about it. If one of us told you that a daughter of ours just ran the 100-meter dash in 10 seconds, what would you know? Nothing! You would only be able to evaluate that fact if you knew the world's record for the 100-meter dash is now under 9.7 seconds.

In other words, to evaluate your portfolio results, you have to compare it with something. There are many ways to do this. You should expect a comparison of your portfolio performance with an important goal such as your financial independence analysis.

By the way, the lack of this precise reporting is one reason we believe brokers and bank trust departments make poor advisors. (This may be changing, so keep an eye out. Even if it does change, there are still plenty of reasons to avoid these folks, as earlier discussions have elaborated.)

How Often Should You Get Reports? Custodian reports should be received quarterly or more often. Most brokerage custodians, such as Charles Schwab, deliver reports monthly. These reports should be regarded as snapshots of your holdings. The report will tell you every cent that came in or out of the portfolio and should value the holdings at the end of the month. However, brokerage reports do not indicate performance. Because some mathematical juggling has to be completed to calculate performance, the advisor should do this.

The advisor's report should be given less often than monthly. We prefer semi-annual reports. We are not uncomfortable with annual reports. The reason not to report too often is it sets up a false expectation and unnecessary anxiety.

Frankly, it doesn't matter much what happens in a particular quarter, because long-term trends cannot be discerned and there's not much of a conclusion. It takes time for a portfolio to be evaluated. This is one

of the major behavioral pathologies of clients. They get anxious if too much time goes by without an assessment. But, a focus on the short-term can be deadly for your investment health. Semi-annual reporting is a good compromise.

Other Services

Advisors who practice as wealth managers or financial planners often offer services in non-investment areas. Some offer tax services. Some offer estate planning. There are many ways to handle these services. Many small advisors refer these services out because the advisory firm can only develop so much expertise. Larger firms can do more services in-house.

Even if the services are referred out, a good advisor will have a well-grooved relationship with the outside professionals and may get involved in the preliminary work. After all, the advisor already knows a lot about you. It can be very cost effective for your wealth manager or financial planner to communicate the necessary information to the other professional.

Make sure you understand the compensation for these other services. Be wary of insurance services. This generally means an advisor compensated by commissions. Be careful.

Estate Planning. There are different ways to handle this facet of the relationship. For example, we give the client a brief tutorial on estate planning—how property passes at death, how property can be titled, and estate-tax savings techniques. Then we assist the client in choosing executors and trustees and in articulating their detailed objectives regarding their heirs. These are not legal decisions, but personal and financial decisions.

We then pass all this on to estate planning attorneys. With some, we have pre-negotiated "discount" fees on behalf of our clients. A discount is obtained because we save the attorney a lot of work by our preliminary activities. The attorney drafts the documents and then meets with the client to explain them and answer questions.

NARROW THE FIELD OF SEARCH

You now know the territory and have enough money to interest an advisor. You know what services to expect. How should you organize your search? Here is a brief outline:

Collect information by calling or writing prospective advisors.

- In your first telephone contact with an advisor, always tell them how much money you plan on investing. It will save both of you time if you are below their minimum account size.
- Ask for information to be mailed to you so you can double check that the firm matches your criteria. Ask for its “ADV, Part II” to be included in the mailing. Don’t just skim it. Study the information thoroughly. After all, selecting an advisor is a major life decision. Hard work pays off. Pretend like you were going to be tested on your knowledge.
- Eliminate brokers, money managers and other product salesmen from the search list.
- As best you can, make very sure the advisor offers the architect/general contractor functions of the wealth manager. Sometimes you won’t be able to be sure except by asking for additional information or clarifications. Be leery if you find out the advisor is also fulfilling the

subcontractor function, such as selecting stocks and bonds, or acting as a purchasing agent by brokering stocks and bonds. It’s very hard to expertly perform all those functions. They know this, so advisors who try to fulfill a more narrow function wind up with investment house designs that only have two or three rooms. They simply cannot be expert enough to construct all the rooms a modern portfolio needs.

- Prepare a short list of candidate advisors. If you have done a good job of screening, the list won’t be long.
- Schedule “get acquainted” meetings. If you are married, both spouses should attend. A good advisor will want to meet both clients. Don’t try to finesse this requirement by claiming “you make all the financial decisions.” Advisors know better. Even if it’s true, advisors will want to meet both clients to test the chemistry.
- Before you start visiting, you have some preparation to do. Prepare a good written statement of the important life objectives that your investments serve. Prepare a concise list of your assets and liabilities. Find your latest income tax return.
- Make a copy of this chapter and develop a quick checklist by yellow highlighting the key issues remaining to be resolved.

THE GET-ACQUAINTED MEETING

A prospective advisor should offer a meeting to “get acquainted” at no charge. Meetings are time consuming. Here are some “dos” and “don’ts”, tested in over one thousand get-acquainted meetings. Following them will make the meeting productive and give you the highest possibility of reaching correct conclusions as to whether you should retain the advisor, and whether their firm should accept you as a client. If you follow these rules, the advisor will love you.

I Read All the Material You Sent Me. You will have gotten preliminary information from the advisor. If you are going to take his offer of a get-acquainted meeting, do him the courtesy of reading the advance information. If only one of you reads it, the non-reader will have labeled himself as a “bump.” (See below.)

Why Are You Here? Begin by telling the advisor why you are seeking advisory service. Are you dissatisfied with a current advisor? If so, say why. Are you not accomplishing your goals? Are you confused by all the investment pornography?

Be candid. Let it all hang out. There is nothing the advisor hasn’t already heard. It will be hard for you to surprise her. Knowing “why” will allow her to directly address your concerns. (Would you conceal your symptoms from your doctor?)

I Am Not A Bump! Both spouses should talk. One of you should not sit silently like a bump on a log. A good advisor will spot that situation and try to get the bump to talk. He needs to hear from both of you.

I Want To Retire In Ten Years. Present your goals and objectives. The better you can articulate them, the better the advisor can respond. He wants to know who is living in the investment house. That's why you should make these lists before the meeting. Preparing them deserves your best efforts.

Reveal, Don't Conceal. Don't be stingy with information about yourself. Bring a list of assets and liabilities and any other information the advisor requests. A good advisor won't talk to you unless you allow them to get a good financial "snapshot" of you. Don't make the advisor work in the blind. If you try, you'll find a good advisor won't!

See How Smart I Am? Don't waste time trying to impress the advisor with your investment acumen. He or she will be able to figure out what you know and what you don't know soon enough. You won't be able to fool them. Be willing to discuss your investment mistakes. They know they aren't talking to an investment wizard, or you wouldn't be there.

The Life and Times Of My Investments. Don't waste time discussing the detailed history of why you picked each of your investments and how well they have performed. You don't have to prove anything. And, your advisor probably doesn't care very much. He is much more interested in looking ahead. He doesn't want you to be trapped in the past. If he wants to know some history, he will ask.

Crystal Clear. The advisor should answer your questions and relate the firm's services to your specific situation. She should be open, candid and clear in her responses. If she is not, give her two strikes. The ability to communicate and educate is a major function of an advisor.

What Will Be Done? One purpose of the meeting is to develop a laundry list of services to be rendered and their costs. You should expect to receive schedule and cost estimates. It's OK if the advisor doesn't give you that immediately. She may need to think about it a bit.

Greed. Don't be greedy. Don't expect free advice during this meeting. Just make sure you understand the services to be rendered and their costs. (You may get some free advice anyway. A good advisor almost can't help giving it. It comes "naturally.")

I Hate His Tie Or Her Suit! Test the "chemistry." Interpersonal comfort is important. Not everybody works well together. You must feel comfortable with the advisor. But, don't make the mistake of thinking the advisor needs your business no matter how big a jerk you are. If he or she is any good, they will reject clients with whom they don't feel comfortable. It works both ways.

"We'll Have To Go Home And Talk About It."

Although it is sometimes true, advisors will recognize this statement as the brush-off it usually is. If you don't like something you hear, tell the advisor. In fact, tell them all your reservations and allow him to address them. Many people are reluctant to discuss their reservations. They think they will hurt someone's feelings, or they think they may be "sold."

It is very foolish to hide your reservations. If you allow the advisor to address them, you may find you have misunderstood something. Here is a promise. If you leave the advisor's office without discussing your reservations, it is unlikely you will be back (That's based on our personal statistics of 26 years. Of the prospective clients who left our office having to "think about it," only about 10% became clients.)

Why is that? Because you most likely will not be able to favorably resolve the reservations on your own. The information needed to do so will have to come from the advisor. You will just drift down the road doing nothing, or you may unnecessarily eliminate the best candidate.

Naming your reservations and hearing a response by the advisor does not mean you have to make an immediate commitment. It means you will have been fair to the advisor and to yourself. If you are not then convinced, simply say the following: "I am not sure you have overcome my reservations. I will need to do some more studying. Thank you for your time."

You Don't Want Me as A Client. Follow the above guidelines. If you are unwilling to do so, the advisor will mark you as a potential "problem" client, who won't cooperate, even for your own good. Good advisors avoid problem clients. They can't afford an unsuccessful relationship, either.

OTHER BUSINESS CONSIDERATIONS

By a combination of reading the advisor's literature and the get-acquainted meeting, you should be able to make a decision. Here are a few additional points:

Escape Hatch. The terms of an advisory agreement should favor you. You should be able to terminate your advisor at any time (with fees prorated monthly.) You don't have to "buy" an advisor, just "rent" by the month.

Known By the Government. Your advisory firm must be registered with the U.S. Securities and Exchange Commission ("SEC") or the state of your residence as required. You should be offered a brochure or SEC form ADV, Part II, which will give you lots of important information about the firm.

CFP. Remember what we said earlier. It is mandatory for principals of the firm to have their CFP designations. This designation signifies commitment to the holistic accomplishment of client objectives.

Management Team. If the firm has more than one person who handles client relationships, make sure that a team, headed by a chief investment officer determines your portfolio. You don't want your investment house to be designed according to the whim with whomever you are working. You want the best brains in the firm working for you.

Experience. Pick a firm that has been in business for a while. Let someone else be the guinea pigs for baby advisors.

References. Good advisors will be happy to give you references. Just be realistic in your expectations and use the references in the best way. First of all, advisors are only going to give you references to well-satisfied clients. Ask clients to relate their experiences working with the advisor.

Also, don't ask for references if you are still shopping and are in the preliminary stages of your search. Check references only when the check is the last thing keeping you from retaining the advisor. Be considerate. If this courtesy is not practiced, client references will get a lot more calls, but with many of them being wasted because the callers had other reservations. Getting a good reference didn't make any difference. The only thing accomplished was to waste the reference's time. The Golden Rule works well here.

Lastly, if you ask for references, call them. Out of consideration to their clients, many advisors will speak to them to alert them to your call. They may go to some trouble to ensure their receptionist or others will get you through to them promptly.

FEES

Amount. We recommend not paying more than about one percent annually for wealth management services if your account is above \$1,000,000. On the other end, accounts below \$500,000 may reasonably be charged a higher percentage, but not more than about 2%.

When adding custodial and money manager costs to a one-percent fee, total costs should not exceed 1.5% per year. In our humble opinion, the 2% percent (or higher) annual fees charged for "wrap fee" accounts by brokers are too much. You should benefit from economies of scale. The rate should go down on larger account sizes.

For non-investment services, advisors usually charge hourly fees. The fees will range from about \$75 per hour to as much as \$400. This is not a price quote, just a common range of fees. Every advisor will tell you their fee schedule.

How Calculated? Advisors commonly determine their investment advisory fee as a percentage of the value of the portfolio at the end of a billing period. Expect the fees to be collected at the end of a month or calendar quarter. If monthly, the fee collected would be 1/12th of one percent. If quarterly, the fee would be 1/4th of one percent. Hourly fees are determined by the time spent

and the rate of the person doing the work. Usually each employee who works on a client case has an assigned charging rate depending on skill and experience.

Sorry Virginia, There Is No Santa Claus In Investing. The most difficulty some prospective clients have accepting fees is because they believe there is a Santa Claus in investing. We are often asked: “Why should we pay you fees when we can get advice from our broker by paying the usual commissions?” After studying this paper, you know there are good reasons not to use brokers besides the raw costs.

Even if the costs were low the conflict of interest will still exist. However, often the costs are not low. We have had the following experience many times. The details are different for each client, but the principles are the same. One of our recent clients had been using a broker as an advisor, and finally wised up. He had a three million-dollar portfolio. For various reasons we liquidated the current portfolio.

We discussed whether we should transfer the individual securities to the new custodian (a discount

broker) or liquidate them where they were and transfer the cash. Our client told us the broker told him the total commissions would be about \$25,000. The new custodian charged only \$7,000. The client just about fainted. The client thought he was paying the “customary” commissions all along. Ouch!

We have said it before, TANSTAFL, “There Ain’t No Such Thing As A Free Lunch.” With a fee-only compensated advisor, all fees will be explicit. Brokers’ commissions will always be necessary, but you should get them “wholesale.”

With transaction-compensated brokers determining costs is difficult. Some are purposefully obscured. Brokers are all now sending “year-end” statements summarizing your transactions for the year. Look at yours if you have one. Although you received “confirmations” reporting the commission on each purchase and sale, more than likely you will look in vain for a summary of commissions paid on the year-end statement.

A PARTING THOUGHT

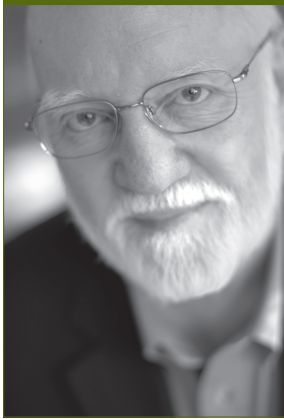
Looking for a good advisor is just like looking for any other professional. There are no guarantees. However, by following the advice in this paper

you will significantly raise the possibility of engaging the appropriate advisor. We wish you success in your search!

ABOUT THE AUTHORS

This paper was first authored by Lynn Hopewell in 1994. At that time, Lynn was President of The Monitor Group, Inc. Lynn attended Old

Dominion University, and graduated from the College of William and Mary, Virginia Tech and Harvard Business School.



Lynn Hopewell

In 1987, Lynn authored a seminal professional paper entitled “Making Decisions Under the Conditions of Uncertainty.” Propelled by his massive intellect and sense of adventure, and buoyed by his academic and professional experiences in mathematics, statistics and probability, this paper was a wake-up call for financial planners and wealth managers that still reverberates today. Later, he served as Technical Editor of *Dow Jones Fee Advisor* magazine and Editor of the *Journal of Financial Planning*. During his active practice, he was repeatedly named as one of the country’s best advisors by *Worth* magazine.

In 1994 he had been appointed by Governor George Allen to a “Champion Schools” Commission, charged to recommend improvements to Virginia’s public school system. In the same year he was elected to the board of governors of the Certified Financial Planner Board of Standards and served a two-year term. From 1996-1999, as a member of the Governor’s State Council of Higher Education, responsible for the coordination of Virginia’s institutions of higher learning, he served as chairman of the planning committee, member of the executive committee and finally Vice Chairman. Lynn resigned as President of The Monitor Group, Inc in 1999, and became Chairman.

In 2000 he was appointed by the Virginia’s Fauquier County Board of Supervisors to its Historic Resources Committee. In 2001 he served as chairman, and also served on the Redistricting Committee of the Town of Warrenton. He was a member of the board of directors of the Virginia Institute for Public Policy, and helped found The Fauquier Institute, a public policy non-profit organization focusing on local issues. Lynn stepped down as Chairman of the Monitor Group, Inc in 2003.

In October 2004 he was given a Distinguished Alumni award from Old Dominion University for his professional and community accomplishments. In September, 2005 he published *Sprinting Past Our Lives as Boys: Woodrow Wilson High School 1954 Virginia Group I State Football Champions*. This is the story of Wilson’s championship team, on which Lynn played.

In the December 2005, he was honored by the FPA of the National Capital Area with a Lifetime Achievement Award. On March 28, 2006 Lynn passed away.



Glenn G. Kautt
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Glenn Kautt has revised and updated this paper since 2002. In the financial services industry since 1981, Glenn is a Certified Financial Planner™ practitioner. He is an Enrolled Agent, licensed to practice before the Internal Revenue Service. Mr. Kautt is a President's Distinguished Scholar graduate of Purdue University and received his MBA from Harvard Business School. He is a member of the Financial Planning Association ("FPA"), the National Association of Enrolled Agents and a Graduate Fellow of the National Tax Practice Institute. He is an Accredited Investment Fiduciary Analyst.

Glenn is a former Chairman of the FPA of the National Capital Area. He is a member of the Board of Trustees of the Foundation for Financial Planning. He served on the Editorial Advisory Board of the *Journal of Financial Planning*, where four of his professional contributions on advanced planning topics have been published. He is a regular columnist for the industry's leading publication, *Financial Planning* magazine. Glenn authored *Stochastic Modeling: The New Way to Predict Your Financial Future*; co-authored *The Invincibility Shield for Investors*; and contributed to *Secrets of the Wealth Makers* by Michael F. Lane.

He has been repeatedly selected as one of the Best Financial Advisers by *Medical Economics* and one of *Worth* magazine's top advisors. *Washingtonian* magazine named him one of the top 100 financial professionals in the Washington DC area. For the past four years, *J. K. Lasser's New Rules for Estate and Tax Planning* has noted Glenn on their "Top Professional Advisor" list. *Bloomberg Wealth Manager* has listed his firm as a top wealth management firm for the past five years. The Monitor Group, Inc. has been cited for the past four years as one of the "Best Managed" investment advisory firms in an independent survey by a leading accounting firm, an accomplishment shared with less than a dozen firms nationwide.

Glenn is Chairman and Chief Investment Officer of The Monitor Group, Inc. A fee-only firm, The Monitor Group, Inc. manages approximately \$500 million and provides a broad array of integrated wealth management services for over 200 clients.