Feel Confident Talking to an Advisor

WHAT YOU NEED TO KNOW. WHAT QUESTIONS TO ASK.

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Introduction

I think many women assume that managing a portfolio of investments is too difficult, too time consuming or takes years of experience.

My experience with friends is that once they have the tools and a basic understanding of investments, they are much happier investing on their own.

Making investment decisions IS empowering.

However, if you are not interested and would rather have someone else handle investing for you, you will meet with an advisor.

Before you meet with an advisor, be prepared.

There are plenty of "5 questions you should always ask an advisor" lists out there. Some of the questions on my RFP are the same. Questions about the firm and background of the advisor for example.

One of the questions *you* should never have to ask is if someone has your best interests in mind when they recommend an investment. Who is going to say no?

Asking about fiduciary responsibility is another gray area. In the institutional world of investing fiduciary responsibility is a given. Fiduciary responsibility is a regulatory requirement.

Fiduciary responsibility for retail investors is ambiguous.

Assuming fiduciary responsibility for institutional assets requires legal documentation. The documentation describes in excruciating detail what the fiduciary responsibility of the investment adviser is.

For the individual investor, fiduciary responsibility is not required. If an advisor says they are a fiduciary asking them exactly what it means for you.

The guide I have created is based on questions used by institutional investors before hiring an investment manager.

You can benefit from the same questions.

Showing an advisor that you are prepared builds confidence.

When you meet an advisor for the first time you will be asked many questions. The questions will be personal. You may not feel comfortable giving a stranger detailed information.

Advisors and brokers are required to ask the questions in order to comply with the "Know Your Customer" regulations.

Before you meet with an advisor you can ask detailed questions too.

I have compiled a comprehensive list of questions like A Request for Proposal.

A Request for Proposal is an in-depth questionnaire. RFP's are used widely to gather detailed information within an industry, including the investment management business.

As individuals we have a unique challenge. We are asked to trust an individual without knowing much about them or their firm.

You want to feel confident in the advisor you choose. You want to know who the advisor is, how they are going to manage your money and what it is going to cost you.
Sending your current advisor or prospective advisor a list of questions has several benefits:

- You don't have to remember every question
- The advisor has time to answer the questions
- You have time to review the answers and make a thoughtful, informed decision
- Sending an RFP is not confrontational. You are showing the advisor that you are prepared and proactive

I recommend emailing this document before your meeting as it is going to require some thought and time on the part of the advisor to complete.

All the questions are fair game. You may not care that much about how performance is measured but it is important because you want to know that the firm you are dealing with complies with industry standards.

What I am recommending is that individual investors be diligent.

The Financial Industry Regulatory Authority (FINRA) and the Securities and Exchange Commission (SEC) have lots of rules and regulations in place, but the reality is that they cannot monitor every financial advisor.

In addition to the list of questions, I have included a “cheat sheet” of the answers you should expect to receive.

The cheat sheet tells you the purpose of the questions, the answers you are looking for and how to interpret the answers.

The advisor you want to work with is the advisor that has no problem answering these questions.

If you are going to use an advisor, I believe you should know exactly what the advisor is going to do for you.

This is **your** decision.

The questionnaire is available for subscribers on The Modest Economist website at no cost. Go to TheModestEconomist.com to subscribe and download the questionnaire.

FINANCIAL ADVISOR QUESTIONNAIRE
Request for Information (RFP)

Name of Company:
Name of Advisor:
Email:
Phone:

In General

What is your educational background?

How many years of investment experience do you have?

What licenses do you currently hold? Include professional designations (CFP, CFA, CPA etc.)

Are you licensed in every state? If no, provide list of states currently registered in.

Please attach your information from: finra.com/broker check

Client Relationships

How many clients do you have?

How many of your clients are active daily?

How often do you meet with or speak to clients?

Do you have a team? If so, how many on the team? Are they licensed?

What are your total assets under management?

Information about your firm

Is your firm a registered broker dealer?

What is your minimum account size?

Are you restricted to high net worth individuals?

How do you handle conflict of interest situations? (clients best interests vs goals of your company)

Does your employer or firm have sales goals or targets for you?

Who is the custodian for your firm?

What information is available to me online? Can I trade in my account online?

Investment Process and Philosophy

Do you recommend individual stocks and bonds? What is your investment process?

Do you recommend mutual funds and exchange traded funds? What is your investment process?

Do you have a specific buy strategy and a sell strategy? How do you implement buy and sell strategies?

What is your asset allocation process? Do you determine allocations or is it done by an algorithm?

How often do you review individual portfolios? How often do you recommend rebalancing?

How is my portfolio performance calculated?

Do you use Global Investment Performance Standards (GIPS)?

How do you benchmark performance?

Fees and Services

What services do you provide in addition to brokerage services? (Accounting, tax, financial planning, estate planning, etc.)

Provide a breakdown of all the fees I will be charged

Advisor fees (percentage of total assets):

Transaction fees:

Custodial or administrative fees:

Fees from mutual funds or ETF's:

12b-1 fees:

Funds with front end loads: When are they appropriate to use?

Funds with back end loads: When are they appropriate to use?

On average how much do your clients pay in fees, including all the above, as a percentage of total assets?

Any additional information you would like to add?

Signature (Advisor) | Date

Check out your advisor

If asking an advisor to fill out a form is not your style or makes you uncomfortable you have other options. One option is to use the Financial Industry Regulatory Authority (FINRA) website:

www.finra.org/about

or jump to the broker check page:

www.brokercheck.finra.org

RFP Questions with Answers

In this section I have provided the questions, the purpose of the questions, the answers you are looking for and how to interpret the answers.

General Questions

What is your educational background?

Becoming a licensed broker does not require any specific educational background. It is up to the hiring firm to decide if they want to hire someone with or without an education. Most do require a college degree, but it is not mandatory.

How many years of experience do you have?

Experience does count. If your broker was not around in 2008, they have historical knowledge of the financial crisis but have not experienced watching the stock market fall off a cliff. Knowing what to do and how to advise your clients comes with experience.

What licenses do you currently hold?

You cannot assume that the person you are talking to is licensed. You can easily find out on the FINRA site, but I would like to know directly from the advisor Becoming a licensed broker does require taking exams like the Series 7 and the Series 63. Becoming a registered investment advisor (RIA) does not require the same licenses.

Are you licensed in every state?

The reason for this question is, licensing is expensive. You may be talking to an advisor who is only registered in your state, or who has not taken the state licensing exams.
Some firms do try to limit where brokers do business but with electronic communication it is more challenging. No harm finding out.

Client Relationships

How many clients do you have?

I want to know if this person is spread thin by having too many clients. It might be okay when the markets are calm but when things are dicey, and everyone calls at the same time, your access could be limited.

How many clients are active on a daily basis?

One person can only handle so many calls in a day. I want to know who I will be talking to if I call. Will it be someone on the “team” ? Will it be someone less experienced?

How often do you meet with or speak to clients?

If you need to speak with someone frequently it would be good to know if your time requirements are going to line up with the amount of time an advisor has. If you expect to hear from an advisor on a regular schedule, let the advisor know what your expectations are. It is worthwhile to clarify your needs up front.

Do you have a team? If so, how many on the team? Are they licensed?

This is another way of asking who your primary contact is going to be. How qualified is the team to answer your questions and help you with mundane tasks like understanding your statement, accessing your online account, or collecting documentation for tax reasons? If you have specific questions about your portfolio and performance, who is going to answer your questions? An efficient advisor will respect your time and not put you in “call back purgatory” where you wait for days to get an answer.

What are your total assets under management?

Most of the “top” advisors shown in recent Barron’s articles on advisor rankings have high minimum requirements, they have teams and they have hundreds of millions (in some cases billions) in assets under management.

The assets under management generate revenue for their companies. The revenue an advisor generates is one qualification for a “top” ranking. Some advisors offer many other valuable services to their clients in addition to investment advice. It is the combination of the assets under management, the size of the team, the time allocated to you as a client that should all be taken into consideration.

Information about your firm

Is your firm a registered broker dealer?

The reason you are asking this question is that many financial advisory firms are not registered broker dealers. For example, a small advisory firm would not have the resources to register as a broker dealer, so they use a third party like Merrill, Schwab, Vanguard, or any number of large firms as their trading platform. Third parties also provide “back office” functions including statements and documentation.

The issue is that you may think the advisory firm you are working with will provide the information above. When you want to see your information online, you may be on a Merrill platform, or a Schwab platform. This can be confusing as well as annoying. Better to know what to expect.

Who is the custodian for your firm? Are there extra costs involved?

The answer is simple. And you may not care. But you do want to know all the moving parts. The custodian is the entity where your assets are held. All advisors use custodians. One of the differences in custodians is the cost, to you.

What information is available to me online? Can I trade in my own account online?

What information do you need? Basic information includes: the cost basis and current market value of each of your holdings, the size of your positions, the length of time you have held a position, performance information, tax information and dividend information.

What I have seen is multiple on-line locations for different pieces of information. There might be an account page on the advisor’s site AND an account page on the custodial website. You don’t really want to have to figure out what page has what, or spend time going back and forth between websites. Ask to see a “dummy” account set up.

If a day comes when you want to place a trade and you cannot get in touch with your advisor in a timely manner, placing a trade yourself could be important.
You cannot leave a voice message or send an email to your advisor to place a trade.

What is your minimum account size?

Unfortunately, today many advisors have very high minimum account sizes. To be fair, the firm an advisor or broker works for may control the minimum account size. If the minimum is $1 million in investable assets, be wary of the advisor who is doing you a favor by accepting a much smaller amount. You may end up paying high fees but receive no real advice or time from the advisor.

Are you restricted to high net worth individuals?

See answer above.

How do you handle conflict of interest situations (clients best interests vs goals of your company)?

An example would be the recommendation of the advisor to invest in a product that the firm is “pushing.” The recommendation MIGHT fit into your overall strategy and be fine for you, but it is up to you to understand what the investment is, and the risks involved. The conflict of interest is selling a product to you to achieve a sales goal when the product is not “suitable” for you.

Does your employer or firm have sales goals and targets for you?

This is a straightforward yes or no answer. If the answer is yes, you will be more likely to encounter conflict of interest situations.

Investment Process and Philosophy

Investment process and philosophy is not something most individuals focus on. At the heart of investment process and philosophy is having a defined and measured approach to managing portfolios.

How does the advisor come to the decision to include a stock, a bond, a mutual fund, or an exchange traded fund in my portfolio? Does the advisor have “sell” strategies?

You want to know if the advisor is thinking about you and your portfolio.

Asset allocation should be the first thing an advisor discusses with you before making any investments. How much do you want to own in stocks and bonds?

Remember, mutual funds and exchange traded funds invest in stocks and bonds. An example of a mutual fund or exchange traded fund that represents an asset class that is not stocks or bonds is a commodity fund or a real estate fund.

Does the advisor focus on asset allocation (the correct way to approach a portfolio) or is it “hey, let’s buy this stock” and then figure out if it fits in the bigger picture later? Later is too late.

Performance standards for institutional investors are not negotiable. Investment managers are held to specific methodologies and accepted standards. Why should it be any different for you?

If an investment manager makes a mistake in calculating performance for an institutional investor, and I have seen it happen, the manager is responsible. It is far more serious than “oops” or “well, it’s close.”

If an advisor tells you that your portfolio returned 8% and in fact it is 6%, who is responsible?

Fees

Fees are complicated and there is no getting around it. I have provided a worksheet that you can use or send to an existing advisor for fee clarification.

The worksheet breaks down for you the different **sources** of fees and how to add them up.

The reason you want to know the details (minutia) of fees is that there is a big difference between paying 1.50% and paying 4.00% or 5.00% when all fees are considered.

If you are paying a total of 5% in fees it means that you must earn more than 5% just to break even.

To understand how this works let's start with $100.00.

- Five percent of $100.00 is $5.00.
- Subtract the $5.00 from $100.00.
- Now you have $95.00 to invest **after** fees.

A 5% return on $95.00 is $4.75. After fees you do not have $100.00. You have $99.75. You are short twenty-five cents!

For you to "breakeven," that is, to have $100.00 **after** fees, your investments must **earn more than** 5.20%

When an advisor tells you that your performance is 8%, what is the first question you ask?

The question you ask is: "Is the performance before fees or after fees?" Because if it is BEFORE fees, your performance is really 2.8% (8.00% - 5.20%). At 2.8% you are not really making any money and you are about even with inflation.

As a rule of thumb, I would not use a fund that has 12b-1 fees, front end loads or back end loads. You can't change the net expense ratio, but you can compare the net expense ratio of different funds.

This is the part of the questionnaire that will take time to complete. I do not believe that fees are "hidden." At all.

How to calculate fees*

Here are the instructions for completing the fee worksheet.

The worksheet is a template. The information entered is an example. All the examples can be deleted.

You can then enter as much or as little information as you want. The worksheet is designed to break out the costs for advisory fees, stock transactions, bond transactions, mutual fund fees and ETF fees.

- Assumptions on the spreadsheets are based on a $100,000.00 market value portfolio.
- The portfolio holds individual stocks, bonds, mutual funds and exchange traded funds.
- Fees come from many different sources including: the advisory fee, transaction fees, mutual funds fees and exchange traded fund fees.
- You or your advisor must take the time to complete the sample worksheet to calculate the true amount you are paying in fees.
- Most advisors cannot give you one number for all your fees. Calculating fees is a tedious process. Using the sample spreadsheet is the correct way to calculate your fees.

The interactive fee sheet is available to subscribers of The Modest Economist at no cost.

*Go to TheModestEconomist.com to subscribe and download the worksheet.

How can you minimize the total fees you are paying?

- Advisors should NOT be charging you a fee on qualified retirement accounts. Be sure to find out.

- Advisor fees are rarely negotiable. Advisors are looking for high net worth individuals who have investable assets of one million dollars or more. Does the advisor provide other valuable services?

- In a sample portfolio of $100,000.00, 1.50% for an advisory fee sounds like a small number. It isn't. Paying 1.5% on $100,000.00 is equal to $1500.00. I think that is a lot of money.

- Fees on mutual funds vary widely. You must find out if you are in a fund that charges a 12b-1 fee, a front-end load, a back-end load, and/or a transaction fee. With all the options available today there is little reason to pay high fees in mutual funds.

- Not all exchange traded funds are "cheap." Make sure to check the expense ratio.

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I founded The Modest Economist ® in 2016 following a 23-year career at the global investment management firm PIMCO.

At PIMCO I advised institutional clients who invest on behalf of S&P 500 companies, central banks and private pension companies in Latin America, healthcare organizations, insurance companies, endowments, foundations, and multi-employer plans.

In addition to my client responsibilities I led the development of PIMCO's advisory services in Latin America with a focus on central banks and pension plans. I launched the multinational corporate channel and headed the relaunch of the PIMCO secure website for clients. For many years I was a voting senior member of PIMCO's economic and secular forums.

Prior to joining PIMCO I was a fixed income institutional salesperson with E.F. Hutton and Bear Stearns.

I have over 30 years of institutional investment experience and hold an MBA from the Anderson Graduate School of Management at the University of California, Los Angeles. I received my undergraduate degree in economics from the University of California, Berkeley.

The Modest Economist is based in New York City although I divide my time between New York City and Southern California.