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TIP 2 HOW FINANCIAL PLANNERS WORK AND GET PAID

Q. A friend told us about a financial planner who has been around for a long time and seems to have an impressive resume. How can we be sure we are working with a planner who is right for us and will look out for our best interests?

A. Education and experience are important, but a financial planner who looks great on paper still may not be right for you. You need to ask specific questions and be prepared to understand the answers you receive. Several good advisor-interview questionnaires are available from the industry's leading professional organizations. Several sources are listed below in this Tip, under "Interviewing Financial Planners."

Amazingly, people are embarrassed to ask an advisor how and how much they get paid. Don't be. It's your money, so look for the best value in everything you buy, including financial advice.

Seek Out the Expertise You Need

Look for an advisor who maintains a thorough knowledge of the financial issues important to you. If you need an overview of your entire financial situation, consider working with an advisor who has earned the CFP® professional marks of distinction.

Also, look for someone experienced in working with people in your situation, and who truly wants to work with and help you. While many financial advisors focus on serving the wealthy, and impose minimum income levels, investment assets, or annual fees, a growing number of qualified advisors can and will work with you on an independent, commission-free basis.

Look at the Package of Services

One way financial planners differentiate themselves is in how they package and deliver services. Most veteran advisors prefer to work with clients on an ongoing basis. They target clients needing comprehensive financial planning advice and investment management services, meet with them two to four times per year, and may charge annual retainer fees (these fees can be substantial). Clients who opt for an ongoing retainer relationship are referred to as delegator-type individuals. Other planners have begun to work with their clients on an hourly, as-needed basis. Clients who want advice only when they request it, are known as validators or do-it-yourselfers. While the annual retainer-fee scenario may be effective for clients who need or want to turn over the management of their financial affairs to an advisor, many people cannot afford or justify the ongoing fees. To determine which type of working relationship is right for you, ask yourself if you want periodic input to or validation of your financial decisions or full-time financial management. The cost difference is significant, so don't pay for more service and advice than you need. Making mistakes with your personal finances is the most expensive lesson you will ever learn. When you need professional guidance, seek it out and be willing to pay for it.

Consider Compensation

Also important is how an advisor is compensated and by whom. It's imperative that you are aware of how that compensation may affect your relationship with the advisor and the recommendations you receive. Financial planners and consultants, investment advisors, registered representatives, insurance agents, stock brokers, and bank representatives may all be compensated via commissions and/or fees, and often both. Additional information and a series of charts that allow you to compare planners' compensation across various service models and portfolio amounts can be found at http://www.garrettplanning.com.

Commission-compensated advisors.

The oldest and most common form of compensation is commissions earned on the sale of insurance and investment products. Though many honest, qualified advisors earn a majority of their income from commissions, conflicts of interest may arise. These people are paid for recommending and selling products from companies that, in turn, pay them commissions. Consciously or unconsciously, that may influence their recommendations.

It's also important to understand that commissions, fees, and loads generally are not charged as a separate line item, instead being hidden or absorbed into the investment. If you don't normally write a separate check to compensate the advisor, it may seem as if the advice you are getting is free. Of course, it's not, nor should it be. Note: The term *fee-based* is synonymous with *fee plus commission*.

Salaried financial advisors.

If a planner is a salaried employee of a bank, financial firm, or discount broker, they have much less potential compensation conflict. Still, you should always ask about sales quotas, incentives (like bonuses or vacations), or if the advisor in any way is directed to recommend certain financial products over others.

Salaries often depend on an advisor's ability to meet sales quotas; and quotas, incentives, and directives can lead to divided loyalties.

Fee-only advisors.

Fee-only financial advisors are compensated exclusively by fees paid directly by clients. They do not accept commissions or compensation from any source other than their clients. A client writes a check or receives an invoice for the amount to be withdrawn from their investment account to pay the fee. The costs of the advisor's services are very clear. Consequently, the vast majority of inherent conflicts of interest regarding compensation are removed from the equation.

Fee-only wealth managers.

Comprehensive, fee-only advisors traditionally charge a flat fee for the initial comprehensive financial plan, then charge an annual retainer or a percentage of the assets for which they provide ongoing financial management services.

Fees for comprehensive financial planning and asset management typically range from 1 to 2 percent per year on a total investment portfolio. The management fee is debited from the investment account, usually on a quarterly basis. The bottom line is that these advisors attempt to set fee schedules and minimums to compensate them fairly for their time and expertise. Ask yourself, however, if you need all they provide on an ongoing basis. You may be paying for and receiving more than you really need.

Another consideration with asset management arrangements is that the planner may tell you that they are on your side because of the financial incentive to help your portfolio perform well. In theory this sounds good, but you need to make sure you are not taking on more risk than you want simply to make a higher short-term return on your investment portfolio.

For those with sizeable investment portfolios, or individuals in unique or complex financial situations that need lots of hands-on professional assistance, a fee-only advisor working for a percentage of assets or one who charges an annual retainer may be the way to go. These are typically comprehensive, ongoing financial planning relationships, where investment portfolio management, estate planning, and charitable giving all are considered and explored. This approach is most appealing to people who want an all-inclusive financial manager and can afford to delegate management of their financial affairs to that person. If you want this level of service, be sure to ask for both client and professional references. You're thinking about turning over management of your financial affairs to another person. You owe it to yourself to do your homework.

Hourly, fee-only advisors. When a client wants to maintain an active role in and more control over their financial affairs, or doesn't have the big portfolio required by some firms (the typical account minimum for fee-only asset management is $250,000 or more), hourly, fee-only advisors are a good option. Such advisors can provide competent, affordable advice.

Fortunately, many advisors offer their services for a flat amount by the project or the hour. This opens the door to one-time meetings, financial checkups, and the opportunity to get a second opinion before a big financial decision. It also works if you want to develop a long-term relationship, because all charges are on the table and can be contracted on an as-needed basis. The reality is that most people probably don't need or want a full-time financial advisor but would truly benefit from meeting with a planner from time to time. Being able to do so on an hourly, as-needed basis puts you in the driver's seat, letting you determine the scope of engagement.

Interviewing Financial Planners

A list of questions is available on the National Association of Personal Financial Advisors' Web site (http://www.napfa.org). Download their brochure, "How to Choose a Financial Planner," and their interview questionnaire, or use The Garrett Planning Network's "Advisor Interview Questionnaire" (see http://www.GarrettPlanningNetwork.com). Be sure to complete a questionnaire for every planner you interview.

Start your quest by visiting the advisor's Web site. Hopefully, the site will answer many of your questions. An independent advisor's site often won't be as flashy as that of a big company, but ask yourself how much of the big company's content directly applies to the advisor you're interviewing. Don't be fooled by glitzy, grand Web sites.

Also, be wary of advisors whose sites require you to divulge personal information and/or contact information as a prerequisite for access to the information pertinent to prospective clients.

When you find one or more advisors who appear to meet your primary requirements, call them. If you're comfortable in the initial few minutes of the call, ask to meet in person. Beware of the advisor who wants to meet right away unless you have indicated that it's an emergency. That advisor may be too new, too desperate, or too pushy.

Most financial planners and advisors will offer a free initial interview or get-acquainted session. Based on the complexity of your situation and scope of services needed, these meetings can last 45 to 90 minutes. In the meeting, be sure to address the issues that are most important to you first. This will save time for both of you.

The initial interview should provide the following:

- Answers to all the questions on your Interview Questionnaire
- A written proposal or contract that outlines the services the advisor recommends and how, when, and how much they will be compensated
- A list of financial documents and data needed to perform the analysis and provide advice
- A target time frame for when the services could be rendered
- An appreciation for the advisor's professional style and communication and listening skills

Under no circumstances should you start working with an advisor until you're satisfied with the interview process, the recommended services, and the method and amount of compensation. Don't let anyone pressure you, but understand that it's the advisor's responsibility to help you take actions they think are in your best interest.

You also may want to ask the planner how they define success with a client. If the response is "an expected rate of return on the investment portfolio," that tells you the advisor may focus primarily on investments and total return. It's an easily measured yardstick, but at what cost? Did they take unnecessary risks with your investments because the rate of return goal was not appropriate for you? On the other hand, if the advisor defines success "based on the client's achievement of his or her financial objectives," that tells you that they approach client relationships with a holistic or comprehensive view. Many of the benefits of financial planning are intangible. The holistic financial advisor may define success as achieving clients' peace of mind, securing their retirement, or helping them realize their dreams.

Consider asking the advisor for referrals from other clients or peer professionals, and interview those people as well. But keep in mind, advisors will select people who will say good things about them.

If you ask the right questions and hear the right answers, you are more likely to end up with the right planner for you.

Additional information and a series of charts that allow you to compare planners' compensation across various service models and portfolio amounts can be found at http://www.garrettplanning.com.

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