Ten Questions to Ask a Financial Advisor

(before you hire one!)

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Introduction

A Financial Advisor is someone you should trust, someone you rely on in good times and bad, and a person who, presumably, has your best interest at heart. But what do you really know about what Advisors actually do? Are you capable of distinguishing among the many types of Advisors? How would you even know if an Advisor is competent?

If you are preparing to entrust your entire life savings to a single professional, you don't want to get this hiring decision wrong. The consequences are simply too great, and there may not be time to recover from a mistake. The good news is that it's not necessary to know everything about personal finances to pick the best Advisor for you (if you did, you might not need an Advisor!).

What you do need, however, is a rational way to distinguish the "good eggs" from the bad, and it starts with asking the right questions. By being prepared in advance of your first meeting with an Advisor-candidate, you will not only feel more confident in your selection ability, but will likely stay more involved in your Financial Plan after hiring.

The following 10 Questions are only a starting point, but they will steer the conversation away from sales, and towards service, value, and commitment. How an advisor answers these 10 Questions, will give you a better sense of compatibility—both personally and financially.

After each question, I've included guidance on what to listen for (Preferred Answers), as well as general context (Why this is Important).

Here we go…

Question 3: If I live (or move) out of town, how can we maintain a personal feel to our relationship, without meeting face-to-face?

Preferred Answer:

"Regular conference calls, email exchanges, *interactive* technology platforms, and even occasional in-person visits."

In 2016, a fully "modernized" advisory-practice has the capabilities to deliver excellent advice and service, without needing to be physically present with the client. While meeting face-to-face is still the most preferred method of engagement, many clients, especially younger *Millennials*, are shifting expectations.
A good advisor will be able to tell you, and then show you, how he's able to accurately – and *personally* – serve your needs using creative (and even *fun*) technology platforms.

Why this is Important:

First, don't worry! You don't need to be tech savvy to work with cutting-edge financial software. In fact, the very best software and *virtual-meeting* tools are specifically designed for "non-tech" people. Moreover, even old-school luddites are capable of using the telephone (and perhaps *e-mail* too!). Services like *Skype* and *Face Time* have "shrunk the world", and provide a feeling of connectedness, even while far away.

On this note, you may have heard of so-called "robo-advice". Robo-Advisors are *automated* platforms that supplement – and sometimes *replace* – traditional financial advisory services. They cost a bit less and don't require that you meet, or even talk to, a human being. These platforms are designed to provide basic asset allocation strategies using your financial data inputs. If you can log onto a computer, you can get some base-level advice. Many traditional advisors have recently embraced this technology to *supplement* their careful and thoughtful analysis. While these tools are mildly helpful, and certainly inexpensive, they require a lot of learning time, before being safe and effective for planning purposes.

Financial planning is rather complex, and having a professional advisor guide you is most often the prudent move. While there's certainly value in sitting in the same room with an advisor, working remotely can be just as effective. If you happen to move out of town, you don't want the added burden of having to shop for a new advisor. Find one now you can stick with…wherever you go.

Question 4: Are there any costs or surrender penalties for leaving your firm or closing my account?

Preferred Answer:

"No, none at all."

If you aren't satisfied for any reason, there shouldn't be any costs, penalties – or hard feelings – to simply part ways.

Why this is Important:

Certain types of investment accounts and financial products pay the advisor an up-front commission (or "load") in exchange for locking your money up for a specified period. These *liquidity restrictions* often come with a fee or

penalty for withdrawing your money too soon, before the surrender period ends. It's not that these accounts or products are necessarily *bad*, but given the choice of *flexibility or not*, it's best to keep your options open. One way to hold your advisor accountable is through a *fee-based* compensation structure, rather than paying up-front commissions. With smaller ongoing fees, based on a percentage of assets under management, the advisor's interest is more aligned with your performance. These fee-based accounts generally have no cost or restrictions for leaving (they are *100% liquid* at all times).

Question 5: How do you measure performance?

Preferred Answer:

"We measure performance in terms of actual outcomes (i.e. planning results). Good performance, to us, means that your goals and objectives were met with the least amount of risk and cost."

Why this is Important:

When advisors – and some clients – think of *performance*, they often think only of investment returns. But performance reports showing returns (price movements over time) are easily manipulated to fit advisors' agendas. Advisors can select beginning and ending dates to make performance seem better than it actually is. Moreover, many advisors only recommend (propose) portfolio investments that happen to have done well recently, rather than recommend the investments sold to previous clients.

On the other hand, if results are measured in terms of *your needs, wants, and outcomes*, performance is harder to fake. You either succeed at accomplishing your financial goals, or not. You either meet your objectives with minimal risk, or you don't. Your economic prosperity, net of risks and cost, is the better metric for measuring true performance.

Question 6: What's your perspective on risk, and what efforts will you take to understand mine?

Preferred Answer:

"Risk can't be eliminated, but it should be *managed* (along with your expectations). We'll work hard to accurately measure your tolerance *and* capacity for short-term losses, to build a suitable investment plan which maximizes potential *gains* within those risk boundaries."

While those may not be the exact words an advisor speaks, the *spirit* should sound similar. Basically, the advisor needs to articulate a *balanced perspective* of risk, and recognize that many different categories of risk affect investment planning (beyond the obvious stock market risks). Additionally, advisors should not substitute their personal risk profiles for that of yours. An advisor's situation – and professional background knowledge – is likely very different from your own.

Why this is Important:

You're probably familiar with the concept *risk of loss*. This is simply the risk that an investment can decline in value, whether on paper or when you go to withdraw it. *Risk of loss* can also refer to investments that underperform your expectations, or even investments that were never taken

in the first place (*missed* opportunity cost). Beyond considering the potential for losses, a wise financial advisor will consider many additional risks that might prevent you from accomplishing your goals. And there are many: Loss of purchasing power (inflation); low interest rates; fiscal policy shifts (legislative tax changes); geo-political risks (foreign trade imbalances, wars, etc.); living too long (longevity risk); dying too soon (inadequate savings for survivors).

Your *capacity* for risk is discovered through Financial Planning processes, while your *comfort-level* (risk tolerance) can be assessed through questionnaires & software tools. A good advisor will understand *both* in order to know you well, and know how to effectively manage investments on your behalf.

Question 7: How do you handle service requests?

Preferred Answer:

"Quickly and accurately."

You're not just hiring the advisor, but the whole support staff too. Providing accurate and thoughtful financial advice is demanding enough. Trying to do that while also processing paperwork, scheduling meetings, changing beneficiaries, and moving money into your checking account is more than any one person can – or *should* – do alone. It's simply not efficient for an advisor to handle basic service tasks that are unrelated to financial or investment strategies. A "team effort" is vital in that regard. The things to look for, when interviewing an advisory team, are responsiveness, attention to detail, and a systematic set of internal processes for handling service-related issues.

Why this is Important:

Talk is cheap. Ten out of ten financial advisors will probably tell you how great their service is, and how fast they respond to clients' needs. I would. But there's simply no way to prove (or disprove) that in advance. So it's important to discuss *specific* processes, formal policies, and dedicated resources, rather than speak vaguely about best intentions.

For instance, how long before sending an email or voicemail can you expect a call back? For administrative needs, who will be your primary point of contact, someone local or an 800-number? Note that all investment and financial planning related questions should be handled directly by your personal *advisor*. This includes phone calls, review meetings, and financial updates. Good advisors may have many clients, but you should always feel like *your* needs come first (because they do!).

Question 8: Where will my money be held for safekeeping?

Preferred Answer:

"Your investment accounts will be held at _____ [*whatever custody & clearing firm the advisor uses*], but how do you mean "*safekeeping*"? (Answering a question with a question / clarifying)

First, the advisor should tell you the name of whatever custody & clearing firm they use for the type of account you're considering (e.g. Fidelity, Charles Schwab, Pershing, etc.). There's really no right or wrong answer to this, although sticking with a large name you've heard of may make some sense. The custody firm is often where your monthly/quarterly statements come from, and where your actual securities (stocks, bonds, mutual funds, ETF's, cash) reside.

Having answered that, however, the advisor should then clarify what you mean by safekeeping. When you say the word "safe", you may be thinking about the value of your account. Many advisors will assume you're asking *is my account secured if the brokerage firm becomes insolvent?* These are completely different issues, as being protected from the investment brokerage firm going "belly-up" in no way protects you from investment losses.

Why this is Important:

Almost all brokerage accounts are protected by SIPC (Securities Investor Protection Corp.). SIPC acts somewhat like FDIC insurance at banks, but with one key difference: While Federal Deposit Insurance (FDIC) actually protects the value of deposits, SIPC only protects against the loss of securities and deposits, not against their decline in market value. The real safety of your account is mainly determined by the *selection* of investments (usually as recommended by the advisor). So when you hear that your account is protected by SIPC, know that the value of your holdings can still go to zero.

Question 9: Speaking of values, what Values (as in moral codes, ideals, beliefs, ethics, etc.) are important to you and your firm?

Preferred Answer:

There's not necessarily a *right* answer here, but you'll want to listen closely to the advisor's response. It may provide you with a glimpse into the *character* of the people you're about to trust with your money. Hopefully, their values will align with yours, and it's usually good if they've thought enough about it to offer some sort of written *Values Statement*.

Check your spirit (your gut-feeling) to get a sense of authenticity & genuineness… or slyness & pandering. Discern whether you believe the firm actually *follows* these values, or has just gone through the motions to look more trustworthy.

Why this is Important:

Unfortunately, it's not uncommon for firms – especially financial services firms – to publicly say they adhere to noble values, and then flatly ignore them in deeds and actions. Values and morals are part of our very essence, the deep-rooted *core* of who we are as people. Finding an advisor who has *internalized* a set of positive values (knows them by heart and shares them passionately) is a good place to start. Take this part very seriously.

Question 10: What happens if you retire, die, become disabled, or otherwise leave the firm (i.e. what's your succession plan for my accounts)?

Preferred Answer:

"Let me share with you our formal written plan for business continuity, and then introduce you to the people who would take over in my absence."

The advisor's answer should be clear and detailed, naming specific persons to take over in the event he or she departs. Ask for details about the training and background of the person(s) who stand ready to take over, and about how that person will be made aware of your goals, objectives, resources, and needs. If something were to happen to your advisor, you wouldn't want to start from scratch rebuilding your Financial Plan. It's better to keep your Plan progressing forward, and with equivalent care.

Why this is Important:

Some circumstances causing an advisor to leave a firm are pre-planned – retirement, for instance. Others are neither planned nor desirable, such as death or disability. If you sense that an advisor is approaching retirement age, this should be a part of your discussions. It's neither impolite nor discriminatory to ask how long an advisor plans to continue advising you, and important just the same to know whom his/her replacement will be.

Shockingly, most financial advisors either haven't thought much about succession planning, or don't yet have a formal plan in place. Or worse, they do have a plan, but it involves *selling* the firm (and your relationship) to some unknown outside buyer. Sadly, many advisors who fail to pre-plan for business transitions, end up working well past their prime. Sometimes it's to continue earning profits, but other times they aren't sure what else to do. That can put you in an awkward situation.

Make sure your advisor has taken the time to personally develop possible successors – ones with expert knowledge & skills, and who share the firm's core values. If an advisor hasn't planned for his firm's own future, don't let them plan for your future either.