FAMILY WEALTHREPORT

Picking The Best Wealth Advisors From The Rest

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Some big names in the industry have turned their attention to differentiating between advisors who can truly handle the complex affairs of the ultra wealthy, and those who just say they can. There is also a movement afoot to get this information across to the consumer.

This movement is important at a time everyone is going after high net worth wealth, simply by virtue of the fact other areas of profitability are disappearing. Middle class wealth has fallen; investment banking and trading revenues have been hit by the poor economy. And ultimately, wealth management is a sales business, says Doug Black, founder of SpringReef Partners, which means some people will always be tempted to make exaggerated claims.

The size issue

Size is one aspect: before the 2008 financial crash and the Lehman Brothers bankruptcy, size was equated with the safety of an institution. But size has provided no immunity against involvement in some of the most nefarious schemes to hit the privately wealthy, or against regulatory run-ins.

Size also depends on the type of institution as it is meaningless to compare an RIA to a private bank – but would a consumer understand that?

Nevertheless, size plays a part. If one hones in on a particular sector it provides an indicator as to how firms or individual advisors are growing their practices and how popular they have proved in the past. Bloomberg Markets recently released a list ranking family offices by assets under advisement. Interestingly, firms dominating in terms of overall size were units of large banks while smaller boutiques dominated growth (albeit from a lower base).

But such lists are arguably more for the industry's interest than the end consumer's. Meanwhile, there are a number of other lists around such as Barron's ranking of financial advisors, which combines characteristics of size along with "the quality of their practice" and factors such as philanthropy.

Family Office Exchange recently came out with a list of "Leading Wealth Advisors," in an attempt to focus on the qualitative side – the quality of advice. However, Barron's later published findings that, for example, one firm on the list was defending itself against charges by the SEC of artificially inflating performance of a hedge fund.

FOX has tightened up the procedures and given staff extra training in this area, founder and CEO Sara Hamilton told Family Wealth Report, and is implementing regular updates and checks on the information advisors provide. It is also accelerating the implementation of an advisory board to identify candidates for the list.

Black says it's essential to take any conflicts of interests out of such lists. The FOX list is open to member and non-member firms, said Hamilton, and non-member firms currently make up around one third - a figure she expects to decrease over time as more potential candidates are identified. Participants can pay extra to receive extra marketing space on the list – aimed at defraying costs – but participants will remain ranked in alphabetical order, she said.

More clarity needed

In terms of the need for such a list, Hamilton says that only a qualitative approach can really identify which wealth advisors can deliver "consistent, high quality advisory services." It is also aimed at awareness about "integrated" wealth advice.

Black, whose firm assists high net worth families in evaluating and selecting wealth managers for a fee, isn't a big fan of lists in general as he pioneers a personalized approach. He also believes the minimum due diligence before engaging a firm – in his experience – takes at least around 5 hours, and usually much longer. (It's important to note though that lists are not recommendations.)

But he certainly agrees that "the challenge is identifying exceptional wealth advisors – who are experienced in handling the complexities of ultra-wealth and offer integrated advice – from the multitude of skilled salesmen in the industry."

The model

As a basic starting point, it would help if the various models relating to the (very broad) concept of wealth management were better understood. Then a potential client could at least begin from a point where he or she knew which firms offered the specific services required, whether that is a private bank, trust firm, broker, or RIA.

"Investors are very confused about the differences between types of wealth managers, in the same way that they do not understand the difference between a broker and an investment advisor," says Kathleen McBride, founder of consultancy McBride & Company, and also of The Committee for the Fiduciary Standard and The Institute for the Fiduciary Standard.

Like Black, she points to the sales nature of the business. "Titles greatly exacerbate the problem because most financial intermediary titles are meaningless marketing terms," she says.

McBride highlights that a wealth manager or advisor can really be one of three types: a registered investment advisor, subject to the fiduciary standard; a broker, subject to a suitability standard; or a dual registrant, both broker and investment advisor.

In her view, the only way in the US at the moment that someone can guarantee they're employing an investment advisor not a salesman is by going down the RIA route, because, simply, they must act in a client's best interests.

"Among the important differences, if an investor accuses a broker of wrongdoing, the investor must prove the broker did wrong. If an investor accuses an investment advisor of wrongdoing, the onus is on the investment advisor to prove they acted in the investor's best interest - could it be more opposite?" she says.

Black is no proponent of one model over another, saying: “There are wonderful advisors across firms in each business model.” He himself comes from the broker-dealer space (he is a former chief operating officer of UBS’ private wealth management business in the US) but is now a registered investment advisor so as to be able to make recommendations to clients.

However, he stresses individuals must be aware of the models – their various strengths and weaknesses. As such, his process begins with explaining this to clients.

Something interesting has emerged from this: “After talking individuals through the relative strengths and weaknesses of each of the business models, a significant number of my clients want to have a conversation with registered investment advisors. They like the independence, they like the transparency, they like the consistency, they like the client coverage ratios,” he says, and they like to know he has read through the form ADV for them.

This agrees with what Jeff Spears, founder of Sanctuary Wealth Services, told this publication earlier this year: that working to a fiduciary standard should be a competitive advantage but in reality many clients don’t understand the difference and tend to assume all their “advisors” have to meet such a standard.

A “mark of excellence”

Looking to change things in this area though is Advizent, which is trying to level the playing field slightly when it comes to the marketing prowess of Wall Street versus independents.

It is also trying to create consistency in what clients can expect from their wealth manager. As such, it recently brought in industry veteran John Bogle to serve as senior chairman of its independent board of standards and develop a concise set of standards of excellence. Member firms meeting such standards will be able to bear the Advizent “mark”. Every year a third-party will conduct an audit of the potential member firms, with a measurable set of criteria to evaluate each firm against.

In terms of the business model, members will pay an upfront fee, but this will not guarantee them the mark; they must also meet the standards.

Fees

Fees are another issue the industry grapples to communicate effectively on. Black says you can get a better “starting point” from RIAs, which publish their rates, but that the wealth management sector as a whole “really falls down” on giving the total asset weighted cost to the client.

There’s “clearly a lack of transparency about total cost to client,” he says. “And that’s a problem because clients have a right to know exactly what they’re going to pay.”

However he adds that some of the very best RIA firms are “absolutely candid about that,” and will even report net of all fees.

One response to a lack of transparency or comparability among wealth managers has often been that it is not a “consumer good” – it’s a people business. While this is true, it should nevertheless be easy for an individual to select a wealth manager that, at a minimum, is competent and honest, and to understand what services they are getting for what price. To this end, real efforts in the area of transparency and raising standards across the board are to be celebrated.