MOMENTUM IN THE ADVICE MODEL CONTINUES

November, 2017

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Albert Einstein said that the definition of genius is taking the complex and making it simple. Morgan Stanley's departure from the broker protocol on October 30th may do the exact opposite by making an already complex industry more complicated. Ownership of the client relationship and the standard of client care from firm to firm can be perplexing in today's financial marketplace. The broker protocol was established in 2004 in an effort to limit litigation among member firms when an advisor leaves one firm to join another firm.

The "Protocol" allowed for advisors to take a limited amount of information about their client roster with them to establish their practice at a new firm. Advisors who have moved from one firm to another may have been lured with up-front cash compensation, or invested their own capital to start an independent Registered Investment Advisory firm, but core to their move was the choice of a better environment for them to work on behalf of their clients. Firms that are not part of the Protocol have tended to be more aggressive litigators and arbitrators which makes it harder for advisors to leave and take clients with them. Firms who do not participate in the Protocol have made it clear that they (the firm) own the client relationship.

That said, there are many people who are clients of large firms because they enjoy working with an advisor of their choice. The idea that a firm owns that choice obscures matters for both the client and the advisor. However, the threat of litigation may not be enough to dampen interest in advisors leaving, especially for the independent Registered Investment Advisory channel where advisors are held to a Fiduciary Standard vs. the Suitability Standard and the client-advisor relationship has been more warmly embraced. Clients have started to move to this model in large part because they know their advisors must act in their best interest, and they appreciate the differentiator of the separation of their advice from the product manufacturing and custody. RPg Family Wealth Advisory is an independent multi-family office advisory group that provides comprehensive family wealth planning strategies and fiduciary services through a professional cadre of experienced and dedicated financial advisors.

RPg family wealth advisory

Plan Well. Invest Well. Live Well.

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Prior to the watershed announcement of Morgan Stanley leaving the broker protocol, there was already a lot of talk in our industry about the differences between the two legal standards financial advisors and their firms are held to—the Fiduciary Standard and the Suitability Standard. The Department of Labor (DOL) has been actively trying to mandate that anyone advising on retirement accounts adhere to a Fiduciary Standard as defined by the DOL. Currently, only independent Registered Investment Advisors (RIA) are required to act in a fiduciary capacity and it applies to every account type.

The Fiduciary Standard of care is the highest standard of care at either equity or law. A Fiduciary is expected to be loyal to the person to whom he owes the duty (the “principal”) such that there must be no conflict of duty between fiduciary and principal. The Fiduciary Standard is often described as always putting the client’s interest before the advisor’s. It also means disclosing any possible conflicts of interest including compensation related to products or referrals.

Under the Suitability Standard of care, an advisor need only suggest products that are suitable for client objectives, income level and age. Also, possible conflicts of interest are not required to be disclosed. Firms are free to find more ways to monetize the client relationship without paying the advisor, some examples include: trading, spreads on cash, loans, investment management distribution fees, minimum account fees, administrative fees, etc. Firms held to the suitability standard may incentivize brokers to sell particular products during sales campaigns as well.

There’s been a lot of media attention around the Fiduciary Standard as the DOL has been seeking approval of the Fiduciary Standard within the suitability world when advising on retirement assets. We think this is a great idea, but why stop at the retirement account? Wouldn’t it be ideal if your advisor were held to the Fiduciary Standard when considering investments for a joint account, a Trust and/or life insurance and annuities?

Today, clients are aware of the benefits of getting their advice from an advisor who must act in their best interest. However, there’s still confusion as to what type of practitioner they are dealing with, so clients must do their own diligence and go beyond the financial plan and investment allocation into the compensation structure of the advisor they are interviewing or currently working with. At some point, we will have a defining moment when all clients scrutinize the complexity of having an advisor who is acting in their best interest on certain types of accounts but not on others. We believe this will contribute to the continued growth of the independent Registered Investment Advisor industry.

Other factors driving the growth of the RIA marketplace include how clients want to interact with their financial professionals. We are starting to see clients ask if the product manufacturing is separate from the advice and custody. As well, technology is changing the advisor-client interface making it easier for advisors to aggregate all assets for reporting purposes, including integrated financial planning software and sophisticated trading technology, to name a few.

We hope this helps clarify the complexities of the ever-changing marketplace. If you would like to discuss any of these concepts, please reach out to a financial advisor at RPg Family Wealth Advisory. As trusted family wealth advisors who have chosen to operate at the Fiduciary Standard, we are dedicated to helping our clients plan well, invest well and live well.

Please refer to and read important disclosures that follow.

IMPORTANT DISCLOSURES

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Sources: ThinkAdvisor.com; http://www.thinkadvisor.com/2017/10/02/mark-tibergien-looks-to-the-future-of-rias?page=2
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