PFP | Advisors Involved in Financial Planning

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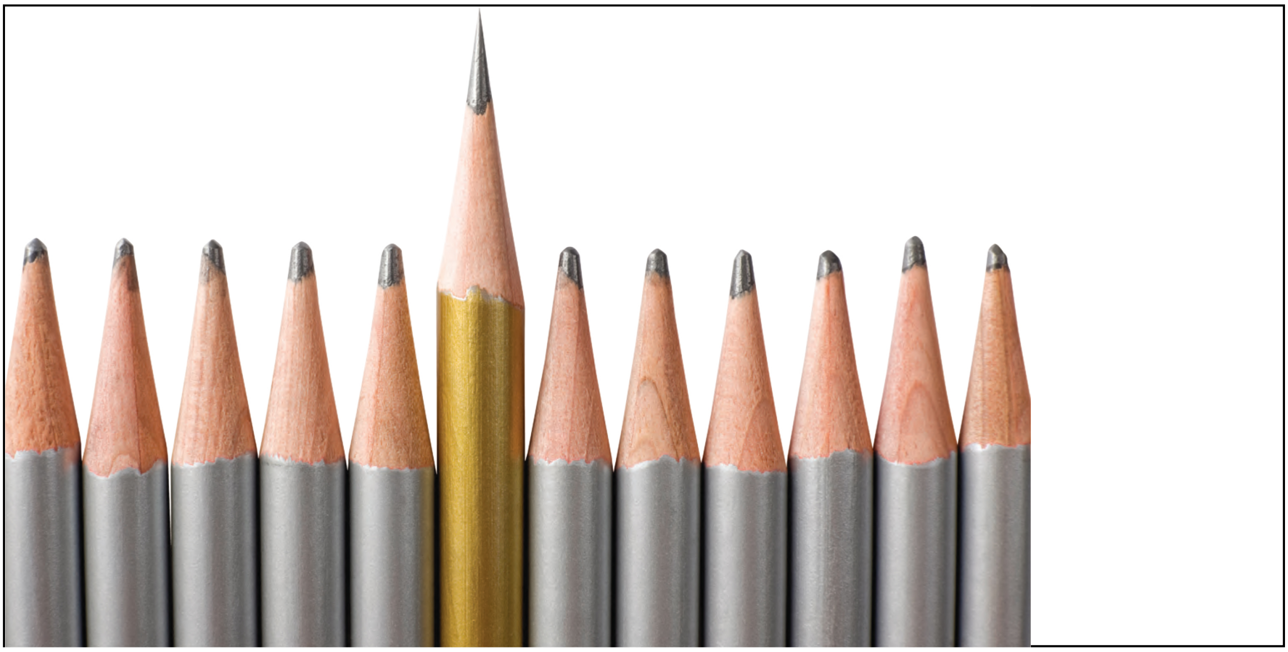
Many CPAs perform financial planning services, as do numerous other types of professionals. This article provides an overview of different kinds of financial advisors and their role in the overall financial planning process. It also covers recent legal developments regarding the duty to act in the client's best interests.

Proposed Regulations

The Department of Labor (DOL) recently announced a proposed Fiduciary Rule that would require financial advisors to consider the best interests of their clients when they make recommendations. Whether promulgated or not, this rule raises the serious issue of whether clients engaging financial planning professionals are being shortchanged or not getting what they expect. In addition, the proposed regulations have opened a floodgate of lobbying against the implementation of the requirements to serve the best interests of the clients.

Those opposed to the rule claim it could change the way they do business, affect their client relationships, and increase their costs. Implicit in their opposition is that it will reduce their revenue. Furthermore, some major organizations have announced plans to sell off parts of their businesses because they will not be able to make money under the Fiduciary Rule.



This rule will *require* financial advisors and brokers handling IRAs and 401(k)s to act in the best interests of their clients. The authors believe this should also apply to all client investment activities and accounts that are provided financial advice. “We put our clients first” is a myth for a large part of the financial services industry, and the DOL wants to make it the reality.

Fiduciary Responsibilities

According to the DOL, most people believe that when they engage an investment advisor, the advisor will act in their best interests. That is not the case, and violations of trust are so egregious that the DOL has proposed regulations to address it. The financial services and insurance industries are very broad, and many people hold themselves out as investment advisors, registered representatives, financial planners, and other similar designations. Many have multiple initialed credentials, supposedly signifying expertise and trustworthiness. In reality, these designations might not mean either.

Financial Professionals

All CPAs can provide financial planning services, and many do, especially in conjunction with tax return preparation. Some of this is incidental to tax advice, and some is offered as a separate service. Furthermore, many CPAs are licensed to sell products, manage investments, or receive referral fees and portions of the income when they recommend a person or organization to a client for such services. There is nothing wrong with this if the CPA is properly licensed, full disclosure has been made to the client, and the services are not performed for an attest client.

While CPAs do not need additional licenses to provide the services incidental to their other services, they will need to be properly licensed if they sell products or manage investments. An estimated 100,000 of the AICPA's 400,000-plus members provide some form of financial planning services. Furthermore, the AICPA offers a Personal Financial Specialist (PFS) designation, with approximately 5,000 members holding that credential. In addition, there are over 10,000 members in the AICPA Personal Financial Planning section, including the PFS holders. The vast majority of CPAs providing these services feel that the CPA license, their additional learning and continuing education, and their experience are sufficient to provide financial planning services. The authors—who both hold this designation—feel confident that this demonstrates expertise to people who are not already familiar with the services CPAs offer.

By way of comparison, the primary certification in the financial planning industry is the Certified Financial Planner (CFP; http://www.cfp.net/) designation, currently held by more than 73,000 U.S. individuals.

A Registered Investment Advisor (RIA) is registered with the SEC and state regulators and can manage investment portfolios and make recommendations of specific investments. Registered representatives usually work for or are affiliated with a broker/dealer who is an RIA and receives commissions on the transactions executed on behalf of customers.

There are also securities licenses needed by those that sell investments. Most common are Series 6, for those licensed to sell mutual funds, variable annuities, and variable life insurance; and Series 7, which covers Series 6 items as well as stocks, bonds, and options.

The National Association of Personal Financial Advisors (NAPFA;http://www.napfa.org) offers designations and has a referral service.

There are other designations and organizations that provide designations and offer referral services and continuing education. Additional designations include MBA, Enrolled Agent (EA), Chartered Financial Consultant (ChFC), Chartered Financial Analyst (CFA), Accredited Investment Fiduciary (AIF), Certified Investment Management Analyst (CIMA), and Chartered Life Underwriter (CLU). Attorneys also provide financial planning services. Not every financial planner offers a full range of services, and many specialize in certain areas.

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Most of the licensing bodies have codes of ethics, professional continuing education requirements, and a means to settle disputes. Some are registered by the state, such as CPAs, or the federal government and thus must adhere to more rigid standards. Many RIAs are required to file a Form ADV with the SEC and state securities agencies. This form provides information about the investment adviser's business, ownership, clients, employees, business practices, affiliations, and disciplinary actions of the advisor or its employees. It also contains narrative brochures that include the types of advisory services offered, their fee schedule, conflicts of interest, and educational and business background of management and key personnel. This is a primary disclosure document that investment advisors provide to their clients. Form ADV is public information, and clients can request the Form ADV if it has not been provided to them.

Compensation

There are many ways that financial planners can be compensated: by the hour; by fixed fees for the engagement, project, or time frame; by the assets under management (AUM); by commissions for products sold; and myriad alternatives. "Fee-based" describes arrangements where financial planners are paid a percentage of the AUM. The percentages can vary from 0.5% to over 2.5% depending upon the size of the account, the services provided, the type of investments, and the activity. Fee-based managers usually do not sell products or receive commissions.

The Client's Best Interests

At present, not all investment advisors are required to act in their clients' best interests, nor to act with a fiduciary responsibility. The industry and professional organizations simply do not define their role in this manner. This is further exacerbated by uninformed consumers who either do not know where to go for professional advice or assume that services performed in conjunction with the sale of financial products are cost-free. For example, a person with four or five designations who sells mutual funds and annuities, when asked about an annuity, would have no responsibility to perform a full-blown financial plan to determine suitability. The customer, however, might assume that the advisor would be acting in his best interests, when in reality the advisor would recommend products that might not be appropriate for an IRA or 401(k) plan. Likewise, a customer might ask about an investment that provides guaranteed lifetime cash flow and be offered an annuity without understanding what happens with the investment principal if she dies precipitously. In neither case would the advisor be doing something wrong, but the appearance and expectation could be that this is a different service—one that carries a fiduciary responsibility.

At present, many advisors who pocket high fees and commissions by selling unsuitable products are following the standard practice of their "profession." The SEC and industry associations make clear distinctions between acting in the best interests of customers and acting as a marketer, but the public does not distinguish between them. Another, perhaps greater problem is the lack of information available to educate the consumer about these distinctions. From the personal experience of the authors, most of the appropriate customers for financial planning services decline them because of the added fees; they do not value independent, unbiased advisors assisting them with determining their goals, developing the plan, overseeing the implementation, and monitoring the performance. That is the client's loss, and no DOL promulgation can change this mind-set. It is up to CPA financial advisors and their professional organizations to promote the value of these needs.

Questions Clients Should Consider

Clients should be the primary concern. Unbiased honesty and transparency will create trust between advisor and client. CPA financial planners should push clients to ask questions and help them determine the answers.

- How is the financial planner compensated?
- Who provides the compensation?
- If compensation is provided by persons referred by the financial planner, will that be disclosed along with the amount or basis?
- If compensation is paid in forms other than direct payments, will that be disclosed? (Note that this is more difficult for the client to oversee. It could be in the form of cross-referrals, consulting fees for assisting with the engagement, hiring relatives for no-show jobs or higher-than-reasonable compensation, travel bonuses, and even free or reduced office rent.)
- Does the professional hold themselves at all times to a fiduciary standard to always make recommendations they consider in the best interests of their client? What does the professional mean by calling himself a "fiduciary"?
- Are full comprehensive financial planning services provided, or are the services limited to executing orders, selling products, and managing investments? (None of the latter services are inappropriate as long as the role and compensation are clearly identified and the client is not expecting anything else.)
- Does the financial planner offer a full range of planning services, or does she specialize in certain areas?

- If the planner offers multiple services, does compensation vary based on the service?
- Is the advisor clear on the client's goals and will they act to the best of their ability to help the client achieve those goals?
- Will the financial planner assist the client in developing an investment policy statement? (See “Helping Individuals Determine Their Investment Goals,” *The CPA Journal*, January 2016, http://bit.ly/2aKvUxM.)

The Unique Value of the CPA Financial Advisor

While many CPAs offer financial planning services, so do many other types of professionals. In the marketplace, CPAs must distinguish themselves by using and adhering to the profession's codes of ethics and the mantra that client's best interests come first. It is important for CPAs to communicate the differences between themselves and other professionals and why they are the best choice.

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