# Why Hire a Fiduciary Advisor?

Red Paper

## Introduction

Making long-term decisions about money can be difficult and even a little scary. Many people turn to an advisor for help with their financial decisions. Many advisors offer good advice but deciding whether they're worth the price can be difficult. Before an investor hires an advisor, they should make sure that the advisor has their best interests in mind.

There are many benefits to hiring an advisor as they often have a broader, deeper knowledge of money management, taxes, social security and insurance allowing them to help investors figure out their savings strategies, retirement options, and overall retirement plan. A professional opinion can be especially helpful towards the beginning of the retirement planning process when most people are trying to set new goals.

Very few investors know the critical importance of selecting an advisor that operates as a fiduciary. Advisors come in all shapes and sizes, from a lower quality sales representative that sells products for substantial commissions, to a fiduciary that solely has the investor's best interests in mind.

## What's a Fiduciary Advisor?

The Securities and Exchange Commission ("SEC") identifies a financial or investment advisor as either a Registered Investment Advisor ("RIA") or an Investment Advisor Representatives ("IAR"), carrying a Series 65 license or in some cases the Series 66 license. By law, advisors with these licenses must act in a fiduciary capacity. They are independent and frequently use job descriptions such as: Financial Advisor, Investment Advisor, Financial Consultant, Financial Planner, or Money Manager. Most importantly, they acknowledge they are a fiduciary when they provide investment advice and services for an amount the client must understand and agree to. RIAs and IARs are held to the highest ethical standards in the industry. They are the only professionals who can provide financial advice and ongoing services at a reasonable expense and they are required to put the investor's interests ahead of their own.

All advisors at Redhawk Wealth Advisors, Inc. serve in a fiduciary capacity and we have developed key principles to guide advisors when acting as a fiduciary. The principles are collectively called our Fiduciary Promise (see picture to the right) and each advisor goes through an education process and formally commits to uphold these covenants.

Fiduciaries are regulated under the Investment Advisers Act of 1940 and are held by law to the highest standard of responsibility to their clients, therefore requiring them to always act in their clients' best interests. This encourages a unique level of personalized service not always found in investor-advisor relationships. The fiduciary duty is a well-established legal principle, backed by decades of precedent. A Fiduciary will have an agreement that lists the services they will provide, the terms and conditions of the relationship, and the costs. If an advisor isn't willing to put their services in writing and disclose their pricing structure, walk away!

## What's a Non-Fiduciary Advisor?

Financial professionals that are not required to act in their client's best interests are sales representatives and hold securities licenses, such as Series 6, 7, and/or 63 which limits them to selling investment products for commissions (see our "7 Reasons Why Variable Annuities are Horrible for a 401(b) or 457 Retirement Account" for more information). Many of these advisors sell the product that pays them the highest commission versus placing an investor in an appropriate investment that's in the investor's best interests. This creates an enormous conflict of interests because the commission is paid by the investment company!

Many brokers and insurance agents call themselves "financial advisors" or "financial planners," but they do not have a fiduciary duty and in fact they aren't required to put the investor's interests first. A non-fiduciary advisor primarily represents themselves or their company, rather than a legal responsibility to act in the investor's best interests. Instead, they only provide the investor with "suitable" financial products. This "suitability standard" is very broad and difficult to impose. Fiduciary duty is stricter than the suitability standard. It's not enough for an advisor to just provide "suitable" recommendations; they must provide the best advice possible.

It is critical that an investor finds out if an advisor is willing to act as a fiduciary. Fiduciaries are required by law to recommend investments in the investor's best interests, not their own or what their firm is telling them to sell. The critical question an investor should be asking themselves is if they want a sales representative investing assets that will impact their standard of living during retirement and their financial security late in life?

## Key Questions to Ask an Advisor

1. **How are they paid and how much?**

   An investor should always ask an advisor for a clear explanation of how they are compensated. The advisor should provide an honest and straight-forward answer. They shouldn't avoid the question, tell an investor not to worry about it, or imply that services are free or are paid for by some other entity.

   All the compensation an advisor receives should come directly from the investor. Any other sources of income should be fully disclosed including any potential conflicts of interests. Investors

need to be aware that advisors that don't act as a fiduciary can earn commissions on trades, trail commissions on mutual funds and annuities, and bonuses tied to their firm's proprietary investment products or trading. These other sources of income are a huge conflict of interests.

In general, the annual costs for an advisor has historically hovered around 1 percent of assets under management. Prices may vary based on the overall services the advisor is providing and how often they are meeting with the investor. It's important to note that advisor compensation structures vary, and some advisors charge for services, collect commissions, charge an hourly rate, or percentage of account value. Everyone needs to get paid for their work; otherwise, they will have no incentive. That said, the client or investor also needs to know the full financial impact, costs and targeted performance, before agreeing to hire an advisor.

## 2. What is their background?

Before people make a major purchase such as a car, television, or refrigerator, it's likely they've done some research to ensure they are making the right decision. One of the most important decisions that any person can make is choosing the right advisor to work with.

Many advisors have advanced degrees in business and finance and years of experience as investment analysts or traders at major financial firms. Be wary of an advisor with little or no previous experience outside of their years in brokerage and/or insurance sales. They lack the overall experience and education of providing an investor with the solutions that are in their best interests.

It's amazing that with all the fraudulent and deceptive money-making schemes in the headlines that only 1/3 of people that decide to work with an advisor do not check the background of the person that they are getting ready to hand over their life savings to! It's very important to check the advisor's background; it may not be an air-tight prevention method, but an investor can easily find out if the advisor has any prior wrong doings on their record.

Here are some sources to conduct a background check on an advisor.

- *Financial Industry Regulatory Authority ("FINRA"):*
  A non-fiduciary advisor that is a registered representative is regulated by FINRA. To help investors keep tabs on advisors, they developed a service called FINRA BrokerCheck that is located at https://brokercheck.finra.org.

- *Securities and Exchange Commission ("SEC"):*
  A fiduciary advisor that is either an IAR or RIA is regulated by the SEC. An investor can go to the SEC web site located at www.adviserinfo.sec.gov/iapd to find out more about the advisor.

- *Certified Financial Planner Board:*
  Before choosing an advisor, an investor should consider if they are a Certified Financial Planner™ professional ("CFP"). CFP practitioners agree to abide by a strict code of professional conduct, known as CFP Board's Code of Ethics and Professional Responsibility, which sets forth their ethical responsibilities to the public, clients, and employers. Investors can go to www.cfp.net to find out if the advisor has had any disciplinary actions against them.

## 3. Will they manage my investments?

An advisor that is acting in a fiduciary capacity will usually select a professional money manager to manage their investments in accordance with the investor's personality (for further information on investor personality, see our "What's an Investor Personality" Red Paper). Additionally, they will place the holdings with a reputable custodian in a discretionary account, so they can make decisions on the investor's account that are in their best interests.

An advisor is a lot like a general contractor. They understand their client's needs and hire sub-contractors who are experts in their field and are highly specialized so that their client is getting the best service for that piece of what they are building. It's impossible for the general contractor to be the best plumber, welder, or HVAC person. It's the same for an advisor. Real fiduciaries will hire the best money managers for their client's portfolios. As in the case of the general contractor, for the fiduciary advisor it's impossible to be the best planner, money manager, or trader, and so on.

## 4. Do they have any conflicts of interests?

An investor should ask the advisor for a copy of their Form ADV Part B. The Form ADV Part B is the uniform form used by advisors to register with both the SEC and state securities authorities. The Form ADV Part B is the primary disclosure document that advisors provide to an investor. It will disclose possible conflicts arising from securities trades and answers a lot of other questions.

As a fiduciary, an advisor owes an investor undivided loyalty, and may not engage in activity that conflicts with an investor's interests without the investor's consent. The United States Supreme Court held that advisors have an affirmative obligation of utmost good faith and full and fair disclosure of all material facts to an investor, as well as a duty to avoid misleading them. An advisor must disclose all potential conflicts of interests between the advisor and investor, even if the advisor believes that a conflict has not affected and will not affect the advisor's recommendations to the investor. This obligation to disclose conflicts of interests includes the obligation to disclose any benefits the advisor may receive from third parties because of recommendations to investors.

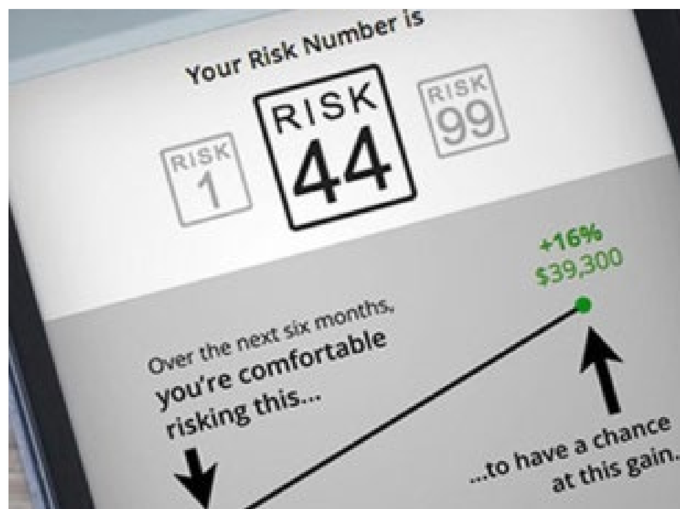
5. **Will they meet with me and for how long?**

Good advisors are great communicators, but at the same time, they only have a limited number of hours. The exceptional advisors segment their clients depending on the list of services each client selects. For clients requiring many services and attention, they may meet with them monthly or quarterly. At a minimum, an advisor should meet with their clients at least once per year or when a client has a significant life change, such as a marriage, death, new job, child, or grandchild.

The length of meetings is also worth discussion. A brief update may be all that is required to put an investor at ease that their assets are being taken care of. This could also be important for newer or younger investors just becoming familiar with an advisor's style or the financial markets in general. Other investors may appreciate in-person meetings at the advisor's office or a lunch or dinner meetings.

## Our Risk Management Approach

Managing risk in an investor's portfolio, as well as managing their expectations about risk, can be very challenging. When markets are up, investors want to know why they aren't doing better (which would require more risk than may be appropriate for their portfolio). Conversely, when markets are down, investors want to know why they're losing money (which would require less risk).

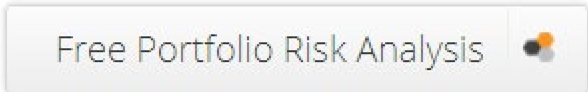



Our first step is to have investors answer a 5-minute online questionnaire that covers topics such as portfolio size, top financial goals, and what they're willing to risk for potential gains. Then we'll calculate their customized risk number between 1 and 99. This number pinpoints their exact comfort zone for downside risk and potential upside gain. The lower their score, the less risk they're willing to accept. The higher their score, the more risk they can handle. Once we know their risk number, we then create an investment portfolio that aligns perfectly with their risk tolerance and goals.

In addition, we can also use the tool to analyze the risk tolerance of an investor's portfolio. Together, we can run stress tests to see how their investments would fare if there were an interests rate spike or an economic crisis. When it's all said and done, investors feel confident that their portfolio matches their personality and needs.

## What's your Risk Number?

We strongly feel that it's important to quantify the amount of risk investors are taking and compare it to what they are comfortable with over the next six months. Click on the icon below to get a free portfolio risk analysis.

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Redhawk Wealth Advisors, Inc. is an SEC registered investment advisor (RIA) that provides comprehensive retirement plan and financial planning tools and critical back-office support for advisors nationwide. Redhawk's focus is to enable advisors create, grow and manage wealth through a broad range of financial products and services that promotes the economic well-being of our select group of clients and advisors.

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