Ten Things Your Financial Planner Won't Tell You

By Nkiru Asika Oluwasanmi

1. "I got this gig on a whim."

There's a huge market of consumers desperately seeking financial guidance these days — and a wealth of planners eager to serve, thanks to an explosion in the financial-planning industry. Ten years ago only about 25,000 people called themselves financial planners, according to Boston-based research firm Dalbar, but today that number has climbed to 650,000.

The reason? Anyone can hang out a shingle and call himself a financial planner: There's no required training or experience. These days bank-employed pitchmen are called "personal financial consultants"; brokers are "financial planners"; insurance salesmen are "financial advisers." "The bulk of people who market themselves as financial advisers are salespeople," says the Consumer Federation of America's director of investor protection, Barbara Roper.

How can you be sure you're hiring a qualified pro? You can start by narrowing the field by sticking to one of the 38,000 Certified Financial Planner licensees (see www.cfp-board.org). A license requires three years' experience and passing a comprehensive, 10-hour exam. Next, grill candidates on how much real planning they've done. Brookfield, Wis.-based CFP Jim Cantrell says he's met advisers who claim to have 10 years' experience, "then you find out that they became a planner only a year ago and spent eight years as a bank manager."

2. "I'm a jack of all trades and master of none."

James Eccleston, a Chicago-based securities lawyer, recalls a client of his who met with disaster through a financial adviser last year. The planner had failed to advise this client of the tax ramifications of exercising stock options, convincing him instead that this was a great opportunity to buy a second home, using the stock as collateral for the mortgage. "And the coffin was sealed," says Eccleston, "because this was a 100% position in Cisco." When Cisco stock tanked, the client's portfolio plunged from $1.7 million in June 2000 to about $5,400 in April 2001. He was forced to liquidate all his shares and take a $100,000 second mortgage on his primary home to meet margin calls. And he got whacked with a $400,000 tax bill.

A good financial planner should work alongside outside professionals — accountants, lawyers, insurance brokers — to offer you the best service. However, at some firms, like the one Eccleston's client used, the planner tries to do everything. Beware. "If they're claiming that they have the expertise to do it all, I would seriously question that," says Roper.

Along with tax planning, estate planning poses great risks, says Eccleston, since flaws might not show up until the client retires or dies. His advice: Double-check anything an adviser says about taxes or estate planning with a lawyer or CPA.

3. "I have ghostwriters draw up your plan."

So you met with a planner, outlined your goals and left feeling that your financial future was in good hands. It might come as a disappointment, then, to learn that this wonderful planner won't be finishing the job. Outsourcing plans to a secondary firm or freelancer is a growing trend, especially among big firms, enabling planners to spend more time wooing new clients. "It's the current corruption in financial planning," says John E. Sestina, co-founder of the National

Association of Personal Financial Advisors. But when a plan is done by outsiders, Sestina says, the information gets stale; there is less intimacy and more room for error. "You can't act on issues as soon as they crop up."

And don't assume the planner will offer up this detail without prompting, says Sherry Hazan-Cohen, a Plano, Tex., CFP who says she doesn't outsource. "[There's] no need for the client to know."

4. "I'm a high-pressure shill in disguise."

The majority of financial planners work on commission, which doesn't make them bad people but can make for bad financial planning. When Irvine, Calif.-based CFP Scott Dauenhauer worked as an adviser at a few big-name brokerage firms during the '90s, he says he was constantly being pushed into selling the firm's proprietary — and often poorly performing — mutual funds, variable annuities or wrap accounts. "We got pressured to sell them because the payout was higher," says Dauenhauer. "But there was no talk of whether it was right for the client."

To avoid such conflicts of interest, shop for a planner through the National Association of Personal Financial Advisors, a strictly fee-only group (no charge backs, kickbacks, trails or other hidden commissions), with more than 750 members. NAPFA planners have to sign an oath stating that they'll never receive commissions and promising to put their clients' best interests first. Along with having three years' experience, they must take 60 hours of continuing education every two years and submit sample plans for review by other NAPFA members.

5. "I have a loose definition of 'fee-only.'"

As the public's suspicion of commission-driven planners has grown, so has the market for "fee-only" planning. Its popularity has inspired some planners "to clothe themselves in the 'fee' word, "says former NAPFA Chairman Gary Schatsky.

A 1997 survey by NAPFA and the Consumer Federation found that three out of five "fee-only" planners actually earn commissions or other financial rewards for their services. According to the CFP Board, 41% of CFPs call themselves "fee-based," which simply means that they charge you an upfront fee and collect commissions on products they recommend.

To be sure your fee-only planner is true to his claim, ask for a written breakdown of fees and of those associated with each investment product, suggests Virginia-based CFP Randall Kratz. "If someone doesn't have what he makes in writing, I wouldn't work with him," he says.

6. "Once I've done the plan, I'm outta here..."

Financial planners like to give you the sense that they'll be with you every step of the way through important financial decisions. But in reality, many clients find that a once-attentive planner becomes increasingly elusive as time wears on.

When Kratz worked for American Express Financial Advisors a few years ago, he says he adopted more than 1,000 clients who had been discarded, usually because they no longer produced adequate income for the adviser. "Typically, the first year was an intense relationship, but clients complained that they stopped hearing from the adviser after that," he says. The reason? The commissions had dried up — a lot of products, especially insurance products, are based on one year of commissions before they drop off, says Kratz. (Teresa Hanratty, senior vice president at American Express Financial Advisors, says that the company rewards advisers "both at time of sale and for ongoing service.")

To avoid a shutout, ask planners at the interview stage how often you should expect to be in touch. A good reply, says Lynnwood, Wash., CFP Kathleen Cotton, is about four times in the first three months, to hammer out a plan, then at least once or twice a year after that.

"7. ...especially if you're not well-to-do."

The past decade has seen a big push among planners to target high-net-worth clients. Therefore, many planners have a minimum asset requirement — typically, $100,000. Considering that U.S. households have a median net worth of $40,000, that leaves a lot of folks in the cold.

Luckily, middle-class clients have alternatives. The Garrett Planning Network is a national network of 90 planners who work primarily with the $100,000-and-under income set, charging hourly fees for periodic advice. Texas CFP Hazan-Cohen recently launched Dream Achieve Planning Network, a similar ring of fee-only planners. And NAPFA's Sestina has his own network of 30 planners scattered around the U.S.; he says they can even handle some clients on a strictly phone basis.

8. "Confused? That's the point."

Many clients meet with planners and leave with more questions than answers. "It's like going to the doctor — you think you understand when you're there, but then you walk out and think, what was it they said?" says Madeline Moore, a Portland, Ore.-based planner. Unfortunately, this confusion is often deliberate so that the planner can better manipulate you.

Sherry Fabricant, a stay-at-home mom in Plano, Tex., and her husband started investing $120,000 with a financial planner at an area brokerage firm at the end of 1997. The planner told them that withdrawal of funds before a five-year period would incur a sliding fee (5% of assets in the first year, 4 in the second and so on). However, not only did the planner put them in high-fee funds without their understanding, but he didn't explain that with any investment transaction, the five-year restriction would begin anew. "Recently, we made a huge sell and a huge purchase," says Fabricant," and it wasn't explained that our five years would then start over. "She is now filing a formal complaint with the NASD.

How can you protect yourself? Ask plenty of questions and write down the responses, and if you don't get straight answers, move on. "Remember, they work for you, "says Sestina," so if you never understand what they're saying, fire them."

9. "In fact, I don't even understand your plan."

There's a plethora of computer software today designed to help planners with clients' asset allocation, cash flow, retirement planning and so on. These tools make for quick plans but can also cause problems, especially when the planners don't understand how the software works.

When Scott Dauenhauer worked at one major brokerage firm as a financial adviser, he and his colleagues churned out boilerplate documents that, he says, all looked alike and usually had glaring mistakes — from a wrong age (which can render the entire plan wrong), to a misunderstanding of the client's goals. The danger was that most of his fellow "advisers" had little training in planning, "so you have a document that's probably wrong and an adviser who can't tell you why."

Cotton suggests you quiz your planner about any computer-generated plan to make sure he or she really understands it. You could ask, say, whether the software assumes a flat rate of return on investments, or how it deals with taxation issues. You can also test your CFP's plan against the free service at Financeware.com, which analyzes plans using real stock market returns — and is therefore more realistic than the flat rate used by most planners' programs.

10. "Good luck busting me for malpractice."

Since the financial-planning industry is so loosely organized, it's not surprising that there are no firm regulations regarding consumer grievances. The CFP Board enforces a code of ethics, "but given the limitations of a voluntary certification program, it's kind of after-the-fact enforcement," says Roper.

So what can you do if you get cheated? If your adviser, like most, holds a securities license, you go to the NASD. But be prepared to wait. Consider the Fabricants, whose case, like nine out of 10 investor cases, might go into arbitration, which, Eccleston says, takes more than a year. Also, since arbitration can cost between $15,000 and $25,000, it makes sense only if you've lost more than $30,000. The majority of these cases are settled, but for investors who go through an arbitration hearing, nearly 60% recover some dough, and one in five gets legal fees covered too. (An alternative, Eccleston says: mediation, which takes less than half the time and the cost of arbitration.)

If you've lost less than $30,000, start by writing a formal letter of complaint to the supervising manager, then write to the NASD, the SEC or your state securities regulator. You're unlikely to get any money back, says Eccleston, but the adviser might face disciplinary action. To protect yourself in advance, check out a financial planner's record. The SEC has started to list client complaints and regulatory violations on its new Web tool, where you can get details on both SEC and state-registered planners.

This story originally ran on December 18, 2001