# [Know who to trust for financial advice](http://novaktony.wordpress.com/2012/08/14/know-who-to-trust-for-financial-advice/)

*By Tony Novak, CPA, MBA, MT*

*(Reproduced from CBSPhilly at*[*http://philadelphia.cbslocal.com/2012/07/25/3-on-your-side-many-have-no-financial-plan/#comments*](http://philadelphia.cbslocal.com/2012/07/25/3-on-your-side-many-have-no-financial-plan/#comments)*)*

Knowing whom to trust for financial advice is not a simple subject. It requires an understanding of four separate intellectual concepts that must be reduced to simple and clear personal resolutions. Those concepts are:
1. Avoid potential conflicts of interest
2, Use an adviser who has fiduciary responsibility
3. Keep custodianship of money separate from the adviser
4. Understand credentials, competency and experience

Avoid potential conflict of interest
It is necessary to first understand and be able to recognize "potential conflict of interest" in order to avoid it. Most important, it is crucial to understand that your resolution to avoid potential conflict of interest here is not an implied accusation of conflict of interest of any other person. For example, your decision to avoid using your brother-in-law, although he may be an excellent financial adviser, is based on the principle of avoidance of potential conflict of interest and in no way is an accusation against the brother-in-law for having any ill intent.

To apply this concept from a practical perspective, simply eliminate consideration of anyone with whom you have a meaningful relationship other than providing advice. The typical objection is that these are the people who care most about you. It is true that they care, but this also leaves a conflict of interest risk since their feeling of "care" can complicate financial decisions. For example, you should stay away from family members or close associates, elders of your church or other similarly influential people in your life. They certainly mean well but their judgment is potentially influenced by their role and relationship. Use a "plenty of fish in the sea" approach to seek out a clean fresh financial advisory relationship that cannot be unduly affected by other relations.

This also means eliminating from consideration anyone who is paid based on the completion of a transaction. Commitment to the transaction itself creates a potential conflict of interest. Sales people, by definition, have a potential conflict of interest in providing financial advice. This doesn’t mean they don’t give good advice or should not be used to handle necessary transactions, but rather it means that they should not be on your list of candidates for a trusted financial adviser.

It is a simple matter to ask a potential financial adviser "How do you get paid?" yet surprisingly few people understand this important detail. If the only way for the adviser to get paid is to complete a transaction, this is a sales person and not an independent adviser. There is nothing wrong with this method of compensation, just be clear on the difference in the two roles. There will be no problem when part of an adviser’s compensation to come from a commission so long as that commission compensation is fully disclosed, it does not increase your overall cost or lower your overall return, the adviser is adequately paid for not completing the transaction and the commission does not increase the adviser’s overall pay for time invested. For example, an adviser who makes $1,000 when not completing a transaction and $5,000 for completing a transaction does not have a potential conflict of interest if it takes three hours to complete the work without the transaction and another 12 hours to complete the transaction.

Finally, pay attention for signs of not-so-obvious potential conflicts of interest. Some advisers are overly influenced by a specific approach, company, belief or philosophy that their work deviates from the bulk of the evidence on the subject. While it may not be possible to entirely eliminate all potential conflicts of interest, by paying attention and discussing these issues in advance will reduce the risk to an acceptable level.

### Use an adviser who has fiduciary responsibility

Fiduciary responsibility simply refers to the legal obligation to act on your best interest when providing financial advice. Because this concept is for too often misunderstood when it comes to financial advisers, it should be listed separately. It is important to know, at an absolute minimum, that a broker or agent does not have a fiduciary responsibility and they will not be held legally accountable for acting in your best interest under the legal system regardless of what title they put on their business card.

Certain professional roles do carry a fiduciary responsibility. These include Certified Public Accountants (CPA) and independent Registered Investment Advisers (RIA) and Certified Financial Planners (CFP). Changes to organizational oversight of RIAs are now being discussed by Congress as part of the proposed Investment Advisor Oversight Act of 2012. Similarly, changes are being negotiated within the professional industry organizations and the financial planning community that may affect CFPs. This is not meant as a negative comment on these professional designations but the public might simply not be clear on the details of how the RIA and CFP designations and the pending proposals apply to fiduciary responsibility. In contrast, people are generally aware that the CPAs are committed to independence and accountability to the public as the core central principles of their profession.

### Keep custodianship of money separate from the adviser

To keep it simple, your money should not be accessible to your financial adviser. In other words, you should not write your check to "Madoff Investment Company" when hiring Mr. Madoff as your financial adviser. Make sure your money is directly conveyed and held by a reputable organization and that your adviser does not have legal access to that money. The custodian organization should usually be legally and functionally separate from the financial adviser and the custodian is normally a well-known and insured bank, investment firm or insurance company. Following this simple step would eliminate the large majority of all financial scams. Yet it is amazing how many times people are duped into granting an adviser custodian rights to access client funds.

### Understand credentials, competency and experience

These first two items – credentials and competency – can usually be considered together because they both address the underlying skills necessary to provide good financial advice. Much has been published about the pros and cons of various professional designations and there is little use to repeat that information here. The fact is that anyone can put the title "financial adviser" or any other similar term on their letterhead. It is left to the consumer to do the research and understand the distinctions of professional credentials.

Finally, consider the adviser’s experience. The value of experience is most often under-valued by those who do not have it and over-valued by those who do. There is a line from an Indian proverb about a warrior speaking against the tribal elder who advocated for peace: "The value of experience is over-rated, especially by elders who nod wisely but speak foolishly". Many young over-achievers in the technology field today would echo similar sentiments. Yet there is plenty of fact-based evidence that the financial planning instincts of younger affluent individuals are just plainly wrong and misguided. The point is that experience should be considered in the context of the assignment. When selecting a financial adviser, the value of experience would be weighed against the ability to accurately evaluate your situation and apply research-based principles with other personal skills that combine to build a long term relationship based on trust. Shakespeare wrote "Experience is by industry achieved, and perfected by the swift course of time". Who could argue with that? In the end, we’re all experienced.

Keep these four principles in mind when considering the suitability of a potential financial adviser. You want someone who is independent of potential conflicts of interest, holds fiduciary responsibility, works independently from the custodian of your money and has the credentials, competency and experience to deserve your trust.